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UNIVERSITY OF ALBERTA

# JAPANESE FOREIGN DIRECT INVESTMENT:
## Theory, Debates and the Case of Daishowa in Alberta

BY ©
Kimiko Abe

A thesis submitted to the Faculty of Graduate Studies
and Research in partial fulfillment of the requirements
for the degree of Master of Arts.

DEPARTMENT OF POLITICAL SCIENCE

Edmonton, Alberta
Fall 1992

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FACULTY OF GRADUATE STUDIES AND RESEARCH

The undersigned certify that they have read, and recommended to the Faculty of Graduate Studies and Research for acceptance, a thesis entitled JAPANESE FOREIGN DIRECT INVESTMENT: Theory, Debates and the Case of Daishowa in Alberta submitted by Kimiko Abe in partial fulfillment of the requirements for the degree of Master of Arts.

Dr. Larry Pratt

Ian Urquhart
Dr. Ian T. Urquhart

Dr. Michael B. Percy

24 September 1992

# ABSTRACT

JAPANESE FOREIGN DIRECT INVESTMENT: Theory, Debates and The Case of Daishowa in Alberta argues that the development of Japanese foreign direct investment(FDI) since the end of the Second World War had been promoted by domestic factors which emerged from structural changes of the Japanese economy, which were outcomes of the industrial policy of the economic-nationalist Japanese government that led the Japan's high economic growth in the post-war era. The domestic factors were Japan's enhanced resource scarcity, labor shortage, and land shortage. Limitation of the expansion of the pollution-causing industries, which resulted from serious pollution issues caused by the economic growth, was another domestic factor.

However, changes in the international political economy have gradually increased their influence on the development of Japanese FDI since the 1970s, as has the integration of the Japanese economy into the interdependent international economy.

The thesis also argues that the Japanese FDI, which aim to secure raw materials and to transfer pollution-causing industries, has encountered, and will encounter, difficulties in host developed/developing states because of increasing public awareness of environmental issues and increasing importance of the issues in national and international political economy.

The thesis conducts the theoretical and historical examination of Japanese FDI, the study about the FDI of the Japanese pulp and paper industry as an example of the FDI of Japan's resource-consuming and pollution-causing industries, and the case study of the FDI of Daishowa Paper Manufacturing Co., Ltd. in Alberta, Canada, in the framework of the international political economy in the late 1980s.

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Kimiko Abe

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## CHAPTER ONE - Introduction

From the end of the Second World War to the early 1990s Japanese foreign direct investment(FDI) grew steadily. It enjoyed its most rapid and bullish growth in the 1980s; the amount became the largest FDI of any nation, reaching US$ 44.13 billion in 1989, a 29 percent increase from the previous year. Compared with the second largest amount, the out-going FDI from the United Kingdom, Japanese FDI was 25 percent larger, at US$ 8.8 billion.[1] The annual FDI of Japan in 1989 was about 4,413 times larger of the annual outflow in the early 1950s, "less than 10 million dollars."[2] Even calculated based on difference of the foreign exchange rate of the yen to the U. S. dollar, i.e., ¥360 in the early 1950s and ¥180 which was the approximate average of the exchange rate in the 1980s, Japanese FDI was multiplied by 2,206.

Why did Japanese FDI increase so rapidly after the end of the war? How have FDI patterns changed? Are there any relationships between the growth of outward FDI and the historic high speed economic growth of Japanese economy after the war, which Chalmers Johnson calls a "miracle"?[3] How did the Japanese industrial policies of those days exert significant influence on the growth? What developments in the international political economy have influenced the growth? What problems have arisen regarding Japanese FDI in host states? Why? This study attempts to look for answers to these questions.

---

[1] The JETRO(Japan External Trade Organization), 1992 JETRO Hakusho Toshi Hen: Sekai to Nohon no Kaigai Choukusetsutoshi(1992 JETRO White Paper Volume: Investment World and Japanese Foreign Direct Investment, (Tokyo: The JETRO, 1992), 3, Table 1-1.

[2] Terutomo Ozawa, Multinationalism, Japanese Style, (New Jersey: Princeton University Press, 1979), 13.

It is argued that domestic factors which emerged from the Japanese state-led economic growth after the Second World War significantly influenced increases in Japanese FDI. It is further argued that since the 1970s, the integration of Japan into the interdependent world economy, along with economic deregulation in Japan, have been more important.

It is also argued that the Japanese FDI which intends to secure raw materials and to transfer pollution-causing industries has faced, and will face, difficulties. The resource-scarcity of Japan, exacerbated by the state-led industrial structural changes, increased the FDI of Japan's resource-consuming industries. A particular form of FDI, i.e., Development and Import (D & I) which is a way to secure a more stable supply of raw materials, is often adopted. The Japanese government also promoted FDI to secure raw materials for the resource-consuming industries as well as the entire

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[3] Chalmers Johnson, MITI and the Japanese Miracle: The Growth of Industrial Policy, 1925-1975, (Tokyo: Charles E. Tuttle Co., 1982).

Japanese economy. Government-led economic growth with emphasis on heavy and chemical industries resulted in the transfer of pollution-causing industries abroad in the form of FDI. During the era of government-led growth, the government promoted heavy and chemical industries as leading industries under lenient environmental regulations. The industries came to cause serious industrial pollution in Japan. As a result, the government tightened environmental regulations and started to promote the transfer of these industries abroad via FDI of these industries. But such FDI has faced and will face opposition from the residents of developed and developing host states as well as criticism from the international society because of rising public awareness of environmental issues and the increased importance of environmental issues internationally.

The search for answers requires us to describe the historical development of Japanese FDI since the end of the war because significant changes took place in various aspects of FDI for the period being considered. The changes were closely related to the growth of the Japanese economy, which was realized in large degree by government industrial policies. These industrial policies are described. In addition, several important changes in the international political economy which influenced Japanese FDI are be studied.

Along with the description of historical development, the problems faced by Japanese FDI are studied in chronological order. In addition, in order to study the issues confronting Japanese FDI in host states, a case study about Japanese FDI in the province of Alberta of Canada is undertaken. The subject of the case study is appropriate to demonstrate the problematic aspects of the dual purpose of the Japanese FDI, i.e., to secure natural resources and to transfer pollution-causing industries. The case studied herein considers the FDI made by a multinational pulp and paper manufacturer which belongs to both the resource-consuming and pollution-causing industries of Japan.

The political system of the host state involved in the case study, i.e., liberal parliamentary democracy, is important, even if the Japanese FDI which intends to secure natural resources and escape environmental regulations have been made mostly in developing states. Democratic, developed states with relatively easy access to information, such as Canada, are conducive to studying issues pertaining to a particular instance of Japanese FDI including: the balance of bargaining power between the Japanese investor and the host government, and the reactions of the public against FDI in particular industries. In contrast, some developing states may not possess accurate statistics and information about incoming FDI, or are reluctant to publicize negative results such as pollution caused by FDI and public opposition to a foreign presence. These states are afraid of losing FDI subsequent to adverse publicity. In some cases, state authorities oppress their people in order to shut out their criticism of problems caused by the FDI.

In the Alberta case study, interviews from the parties concerned are important sources because of a paucity of scholarly work about the case in the framework of the international political economy. However, interviews inevitably attest to the subjectivity of the interviewees, who give answers selectively and based on perceptions. Therefore, this study uses interviews while taking into consideration the bias of the subjects, and comparing information from other sources.

The second chapter reviews theories of regarding FDI in terms of their specific applicability to Japanese FDI. They include theories which were developed based on studies about features of the FDI of Western multinational corporations (MNCs), mainly those of U.S. MNCs, as well as theories which focus on particular features of Japanese FDI. The relationship between Japanese MNCs and the Japanese government is also studied. In the third chapter, the historical development of Japanese FDI is studied. In the historical context, the influence from the Japanese industrial policy on the development of FDI is defined based on the premise that the Japanese state has led economic growth by revising the comparative advantages of the economy. Influence from the international political economy is also evaluated. A way for the FDI of securing raw materials, i.e., Development and Import (D & I) is also introduced.

The fourth chapter analyzes features of the FDI of the Japanese pulp and paper industry as an example of the FDI of Japan's resource-consuming and pollution-causing industries. The chapter also presents basic information about the Japanese pulp and paper industry and about Japanese government policies toward the industry.

The fifth chapter analyzes the problems faced by Japanese pulp and paper producer Daishowa Paper Manufacturing Ltd. in Alberta. Features and causes of the problems are explored. In addition, through an examination of Daishowa's FDI, the FDI policies of Japanese pulp and paper industry as well as the policies of the Japanese government toward the industry are assessed in the context of the international political economy in the late 1980s. The final chapter summarizes the finding of this thesis.

# CHAPTER TWO - Theories of Foreign Direct Investment

## Introduction

This chapter discusses theories of foreign direct investment(FDI) which were based on studies of Western MNCs. It will also assess the applicability of such Western-oriented theories in a Japanese context, with specific regard to Japanese FDI. Theories regarding FDI "revolved around the behavior of Western multinationals, notably, U.S. multinational corporations, with their Japanese counterparts being treated either as a special case or as mere newcomers who will inevitably follow the same path of the Western multinationals."[1] But such theories have some difficulties in explaining features of Japanese FDI. This chapter also examines the very particular relationship between Japanese FDI and the Japanese government. It is concluded that it is problematic to make generalizations about the influence of Japanese FDI on host states, and the conclusion is substantiated.

## Product Cycle Theory

### (1) Contents of the Theory

There are two important theories which explain the FDI of

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[1] Terutomo Ozawa, Multinationalism, Japanese Style, (New Jersey: Princeton University Press, 1979), 41.

Western MNCs. One of them is "product cycle theory" which was developed primarily by Raymond Vernon,[2] and accounts for the FDI of American manufacturing MNCs as they were made until the 1960s.[3] The theory posits that development of new products is carried out by corporations from states possessing a comparative advantage in terms of advanced technologies, large national markets, and a generally high living standards. Newly developed products can be sold in the national market at first, and exported other industrialized states. Thus, the firms enjoy their monopolistic position in the home- and host-state markets.[4]

However, in the course of time, the technologies developed become standardized and diffused. As a result, firms in other industrialized states come to produce the innovated products by acquiring the standardized technologies, and they start to sell the products in their local markets. They also export their products back to countries where the products were first developed. In order to compete with new producers in the sales of the products, the innovator-firms make the FDI in the new producers' states and sell the products manufactured there. Finally, in order to take advantage of lower labor costs, the innovator-firms make FDI in developing states as well -- a move made attractive by the standardization of technology.[5]

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[2] Robert Gilpin, The Political Economy of International Relations, (Princeton: Princeton University Press, 1987), 234.

[3] Gilpin, 235; Raymond Vernon, "The Product Cycle Model," in George Modelski, ed., Transnational Corporations and World Order, (San Francisco: W. H. Freeman and Company, 1979), 114.

[4] Gilpin, 235.

(2) Applicability of the Theory to Japanese FDI

The product cycle theory "does not directly apply to the case of Japan's manufacturing venture overseas," because Japanese MNCs in manufacturing industries were not innovators of new technologies for many years after the Second World War, but "followers" of the Western product-innovators.[6] Therefore, it is necessary for us to study the theory while taking account of this fact.[7]

The followers enter the later phase of the production cycle in which un-skilled labor in the developing states can handle the standardized technologies for production. In contrast, the innovators hardly employ unskilled labor in the earlier phase of the production cycle because unskilled labor cannot handle the newly developed technologies. This means that labor cost is a principal factor in the later phase of the production cycle, and the research and development cost in the earlier phase. Accordingly, in order to reduce labor cost, labor-intensive Japanese industries make FDI in developing states in which cheaper labor is abundant.[8]

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[5] Ozawa, 48-49; Gilpin, 235-236.

[6] Ozawa, 50.

[7] Ibid., 50.

[8] Ibid., 50.

## Industrial Organization Theory

### (1) Contents of the Theory

Development and diffusion of the new technologies have significantly speeded up since the Second World War,[9] and this phenomenon has reduced the advantages of innovators of new products in their FDI which are expounded by the product cycle theory. Raymond Vernon himself states that the theory started by 1970 to have difficulties in explaining reality.[10]

Because of this theoretical weakness, the industrial organization theory was developed by Stephen H. Hymer, Charles P. Kindleberger, and Richard E. Caves.[11] It is "a more general and inclusive theory of the multinational and foreign direct investment"[12] and a combination of industrial organization and international economic theory. It argues that MNCs possess "firm-specific, rent-yielding attributes such as either superior technology or greater knowledge about production, marketing, and management"[13] which cover the cost incurred from the FDI.[14] In addition, this theory argues that the MNCs make the FDI in an "oligopolistic market structure in both home and host states."[15] The MNCs place production stages in different states; their production stages are vertically integrated. Such a production system enables MNCs to internalize markets and reduce transaction costs.[16]

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[9] Gilpin, 236.

[10] Raymond Vernon, 114.

[11] Ozawa, 42; Gilpin, 237.

[12] Gilpin, 237.

[13] Ozawa, 42.

[14] Gilpin, 237.

Richard Caves underlines that vertical integration can save "the contracting costs and uncertainties that would mar the alternative state of arm's-length transaction" between firms in different states. Long-term contracts might reduce the transaction costs and the uncertainty, but making long-term contracts requires "greater negotiation cost."[17]

The vertically-integrated production system has rapidly expanded intra-firm trade. As a result, "a substantial fraction of global trade has become the import and export of components and intermediate goods rather than the trade of final products."[18]

(2) Applicability of the Theory to the Japanese FDI

There are two features of Japanese FDI which do not fit the industrial organization theory. The large size of MNCs defined by the theory does not accord with the size of most of the small and medium Japanese MNCs which made FDI in developing states.[19]

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[15] Ozawa, 42.

[16] Gilpin, 237.

[17] Richard E. Caves, Multinational Enterprise and Economic Analysis, (London: Cambridge University Press, 1982), 16-17.

[18] Gilpin, 238.

Next, these Japanese small- and medium-sized MNCs do not possess firm-specific advantages. The technologies which they are employing in their FDI are low or standardized technologies. In addition, it is unlikely that the small- and medium-sized Japanese firms possessed marketing and management skills comparable to those of the big Western MNCs. Instead, they were losing industries to foreign competitors because of changes of comparative advantage in the Japanese economy. Higher wages in Japan accompanied with a shortage of young workers weakened the international competitiveness of Japanese labor-intensive industries. A good example of this is the textile industry which made FDI rapidly in Asian states in the late 1960s and the early 1970s.[20]

Why did seemingly "unqualified" Japanese firms make FDI? The reason for this is that the "backward industrial environment" of the developing states gave "quasi-advantages" to the Japanese firms.[21] In addition, the lack of firm-specific advantages was compensated for by the support of large Japanese trading companies(Sogoshosha).[22] For example, the Sogoshosha's global marketing networks, management skills and knowledge of overseas business helped small- and medium-sized firms in their FDIs.[23] It might be said that the economically nationalist Japanese government has also made up for the lack of firm-specific advantages. It supported the FDI of Japanese industries, especially those of the resource industries, in order to secure raw material for Japanese industry as a whole.[24]

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[19] Ozawa, 44.

[20] Kiyoshi Kojima, Nihon no Kaigai Chokusetsutoshi (Japanese Foreign Direct Investment), (Tokyo: Bunshindo, 1987), 98, Table 3-2.

[21] Ozawa, 44.

[22] Ibid., 47-48; the function of Sogoshosha in the Japanese FDI will be studied in the third chapter.

However, the theory does apply to other aspects of Japanese FDI. The FDI of Japan's resource-consuming industries to secure raw materials in the form of vertical integration is interpreted as the measure to reduce "the contracting costs" of securing raw materials and "uncertainties" existing in overseas transactions.[25] The theory also explains to the rapidly-increased Japanese FDI in the United States and the Western European states from the mid-1970s and to the mid-1980s. These foreign investments were mainly made in order to get over the so-called new protectionism against Japan and the newly industrializing Asian states.[26] The Japanese MNCs which made this type of the FDI were large oligopolistic industrial manufacturers which possessed the firm-specific advantages defined in the theory.

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[23] Ibid., Ozawa, 31-32; Kiyoshi Kojima and Terutomo Ozawa, Japan's General Trading Companies: Merchants of Economic Development, (Paris: The Organization for Economic Cooperation and Development, 1984), 24; Tran Van Tho, "Nihon no ASEAN Shokoku eno Chokusetsutoshi: Seizougyo Toshi (The Japanese Foreign Direct Investment in the ASEAN states: Manufacturing Industries)," in Sueo Sekiguchi, ed., Kantaiheiyoken to Nihon no Chokusetsutoshi (The Pacific Rim and the Japanese Foreign Direct Investment), (Tokyo: Nihon Keizai Kenkyu Center, 1982), 61.

[24] The state promotion of the FDI securing raw material will be studied in the third chapter.

[25] Caves, 16-17, 20.

### Macroeconomic Approach

Kiyoshi Kojima developed an "ingenious"[27] theory applicable to some features of the Japanese FDI based on the Hecksher-Ohlin theory of trade. Kojima's theory of FDI is a normative theory which argues that "disadvantaged industries or industries losing their competitive advantages in the home states should make the FDI in actual or potential advantaged industries in the host states."[28] The assumption of this theory about changes of comparative advantages is contrary to that of Robert A. Mundell's theory. Mundell argues that capital flows from a capital-rich to capital-poor states make the host states capital-rich; consequently the host states' capital-intensive industries, which were previously disadvantaged, grow. Along with capital inflows, reallocation of resources occurs in the host states in a way that the resource moves to the vitalized capital-intensive industry and promotes the further growth of the industry. But the less capital-intensive industries in the host states, which were previously advantaged, decline.[29]

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[26] Gilpin, 240.

[27] Ozawa, 56; Peter J. Buckley, "Macroeconomic versus International Business Approach to Direct Foreign Investment: A Comment on Professor Kojima's Interpretation," in Hitotsubashi Journal of Economics, 24 (1983): 95.

[28] Kojima, 24.

On the contrary, Kojima argues that the capital flows from a capital-rich country expand the production frontier of the host state and foster the host state's less capital-intensive industries which are "actual or potential advantaged industries,"[30] whereas the host state's capital-intensive industries, which were previously disadvantaged, decline. Thus, owing to the enhancement of the comparative advantages between the home and host states, "the trade between the host and home states increases and become more profitable to the two sides."[31] The trade consists of export of the less capital-intensive products from the host state to the home state and the export of the capital-intensive products in the opposite direction.[32]

Based on this argument, Kojima defines the Japanese FDI as the "trade-oriented" FDI by which increased the trade consists of labor-intensive products from the Asian host states to Japan and capital-intensive products from Japan to the host states. Kojima defines the FDI by the Western MNCs as "anti-trade-oriented" FDI because, he argues, it decreases the trade between the home and host states. The reason for the decreases is that products from the Western FDI, which came to be produced in the host states by the Western MNCs' FDI, substituted the export of capital-intensive products from the Western home states.[33]

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[29] Buckley, 96.

[30] Kojima, 24.

[31] Ibid., 25.

[32] Ibid., 24-25; Ozawa, 56.

However, Kojima's theory is not applicable to the FDI made by Japanese capital-intensive industries, which have comparative advantages in Japan; the FDI made by them displaces trade of their products manufactured in Japan between host states and Japan.[34]

Therefore, it could be said that Kojima's theory of the FDI fostering less capital-intensive industries is only applicable to the Japanese FDI made in the developing states.

Another important point of Kojima's FDI theory is the role of FDI as a "tutor."[35] The FDI should have a function of "transferring a package of management resources such as capital, managerial skills and technology to the host states" and a function of "improv(ing) the production function of that specific industry" which receives Japanese investment.[36]

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[33] Ozawa, 15.

[34] The FDI of these industries have decreased the trade of their finished products between the host states and Japan, however, trade by the industries has not been substituted completely by the FDI. The parts of their products have been exported from Japan to the host states.

[35] Kojima, I.

[36] Kojima, Gaikoku Boeki (International Trade), 4th ed., (Tokyo: Shunju Sha, 1973), 6-7. quoted in Ozawa, 58.

Kojima maintains that Japanese FDI in the developing states has played the role as a tutor.[37] Japanese FDI has been made by the less capital-intensive industries which were disadvantaged industries in Japan, therefore, according to Kojima, the transfer of the technologies to the host states has been easier.[38] In addition, Japanese FDI has been made in the order that the easier transfer of the production technologies of a Japanese industry was, the earlier FDI of the industry was made.[39] Furthermore, the technological gap between Japan and the host states have been relatively smaller than that between Western states and host states.[40] Thus, Japanese FDI is significantly different in this respect from the general FDI delineated by the theories of Western economists. The theories of Western economists maintain that firms making FDI hold significant superiority in their technologies to the local firms in the host states.

Some economists have criticized Kojima's argument about Japanese FDI's role as a tutor. It might be plausible that the Japanese FDI fostered the economies of host states by transferring technologies and managerial skills. However, it is difficult to argue that those Japanese MNCs who make FDI had the express intention of so favoring of host states. Rather, any beneficial results of FDI for the host states were an incidental outcome of the profit-seeking business activities of Japanese MNCs.

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[37] Kojima, Nihon no Kaigai Chokusetsutoshi (Japanese Foreign Direct Investment), 16.

[38] Kojima, Kaigai Chokusetsutoshiron (Theory of Foreign Direct Investment),(Tokyo: Daiamondo Sha, 1977), quoted in Ozawa, 58.

[39] Kojima, Nihon no Kaigai Chokusetsutoshi (Japanese Foreign Direct Investment), 38.

[40] Kojima, Kaigai Chokusetsutoshiron (Theory of Foreign Direct Investment), quoted in Ozawa, 58.

## The FDI Promoted by the Continual Economic Growth

From the macroeconomic point of view, the main factors which increased Japanese FDI from the end of the Second World War to about the mid-1970s emerged from changes in the comparative advantage of the Japanese economy, and the changes themselves resulted from the strategy of government-led economic growth.[41] The changes should have slowed down economic growth if Japanese FDI had not been made as a countermeasure to overcome their negative effects. The changes are a part of what the classical economists, and John Hicks, see as inevitable impediments to continual growth of economies in the long term.[42] The classical economists, represented by Ricardo, were "preoccup(ied)"[43] with shortage of land as the main impediment to continual economic growth. Shortages of land and those of labor occurred in Japan because of the rapid industrial expansion in the period of high economic growth. The labor shortages were accompanied by the rapid wages increases for Japanese workers. The technological gap between imported technology and indigenous technology, which pulled the economic growth, gradually diminished. Expansion of the resource-consuming heavy and chemical industries contributed to rapid economic growth while exacerbating resource scarcity. These conditions all lead to the continual growth of Japanese FDI.

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[41] Ozawa, 69.

[42] Ibid., 65-66.

[43] Paul A. Samuelson and William D. Nordhaus, Economics, 12th ed. (New York: McGraw-Hill Book Company, 1985), 788.

## Transfer of Problematic Industries

It should be noted that Japanese FDI characteristically seeks to transfer problematic industries abroad. During the period of economic growth, serious industrial pollution was a by-product of the expansion of heavy and chemical industries. Because of opposition from people living close to production sites and tightened environmental regulations, industries, encouraged by the MITI and other agencies of government, sought to employ FDI further to expand production. And the industries made FDI in many host states with lax environmental control standards.

## Relationships between Japanese MNCs and the Japanese Government

When FDI constitutes a significant portion of the host or home economy, or when it is made in industries considered important either economically or militarily, it exerts much influence on home and/or host governments. Therefore, it is critical to study these relationships. The relationship between the MNCs and home/host governments have been studied extensively. Business activities of MNCs consist mainly of FDI, although MNCs in service industries do not practice production. Therefore, instead of relationships between the Japanese "FDI" and the Japanese government, relationships between the Japanese "MNCs" and the Japanese government will be studied herein.

Studies about the MNC-government relationships have been centered on the U.S. MNCs and the home and host governments because of the preeminent status of the U.S. MNCs in size, number, their influence in the international political economy. In contrast, studies involving Japanese cases remain relatively few. Therefore, the relationship between the Japanese MNCs and the Japanese government will be examined through the theories based on U.S. cases.

Robert Gilpin maintains that the interests of U.S. MNCs and the United States are in accord on many points, and the same argument is plausible for Japan. Three imperatives from which Gilpin finds some accord of interests between home governments and MNCs are: 1) securing raw materials, 2) earning foreign exchange reserves, and 3) maintaining economic status.[44]

Gilpin emphasizes the importance of U.S. FDI to the U.S. government as a tool to secure raw materials for military use.[45] Needless to say, Japan also needs raw materials for military, as well as industrial, purposes, but the degree of necessity for Japan has been much lower than that for the United States, which has been involved in wars and military conflict since the end of the Second World War in the so-called bipolar structure of the international politics.

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[44] Gilpin, 241-243.

[45] Ibid., 241-242.

Earning foreign exchange reserves through business activities of the MNCs is important to many states; however, this function became important to Japan relatively recently. It was not until the 1980s that Japanese MNCs came to earn profit from their FDI to such a degree that the account of the earning from the FDI of Japan's balance of payment turned into surplus[46]; Japanese multinationals' profit from their FDI did not contribute to increasing Japan's foreign exchange reserves until the 1980s.

Gilpin also holds that the U.S. government regards American MNCs as an instrument to propagate the ideology of "the American free enterprise system" as "an alternative to the Communist or socialist models of economic development."[47] This argument is plausible and indeed was in a bipolar world. But it does not fit the Japanese case. The Japanese government has not taken actions indicating a desire to make use of Japanese MNCs for a similarly ideological purpose.

The U.S. government also regards American MNCs as an instrument to command diplomacy favorable to itself, Gilpin maintains.[48] The Japanese government dose not seem to take advantage of Japanese MNCs for this purpose. Rather, the Japanese government has made use of diplomacy to secure raw material for the economy as well as for the Japanese MNCs in resource-consuming industries. A good example of this is the "oil diplomacy" in the aftermath of the first oil crisis in 1973.

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[46] Masahiro Kawai and Motoshige Itoh, Kokusai Keizaigaku Nyumon (A Guide to the International Economy), (Tokyo: JICC, 1991), 21, Table, 1.

[47] Gilpin, 243.

Gilpin adds that "as trade barriers have risen, governments have encouraged their own multinationals to invest abroad to help maintain their nation's share of world markets."[49] Japanese industrial manufacturers have made FDI in the United States and Western European states in order to get overcome the trade barriers. But it might be difficult to argue that the Japanese government has encouraged the FDI of Japan's industrial manufacturers in order to keep the national share, even though the Japanese government should have been relieved to some extent by the decrease of trade friction. Instead, it would be reasonable to speculate that the FDI of the Japanese manufacturers has been made by their firm-specific business decisions to maintain the sale of their products in the two regions.

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[48] Ibid., 243.

[49] Gilpin, 244; Gilpin refers to Andrew J. Spinder, The Politics of International Credit: Finance and Foreign Policy in Germany and Japan, (Washington D. C. : The Brookings Institution, 1984).

## Relationship between Japanese MNCs and the Host States

Concerning the relationship between MNCs and host states: the MNCs can exert either a positive or negative influence in the affairs of the host state. The positive influence, mainly related to the economy, includes transfer of technologies to and creation of employment in the host state, both of which improve the economic well-being in host states. The arguments which emphasize the negative influence have centered on the relationships between MNCs and the host developing states. The negative influence, which spreads over the economic, political, and socio-cultural life of host states, includes; transfer of inappropriately high level of technologies, distortion of the host economy or "dependent development"[50] or a "branch plant economy," exploitation of natural resources and destruction of the environment, deprivation of political autonomy as described by Raymond Vernon in Sovereignty at Bay,[51] and the decline of indigenous culture. Some of these conditions may occur even in the host developed states.

However, it is difficult to describe the influence of the MNCs of a particular nationality as either negative or positive. Proving that the U.S. MNCs , for example, exert negative influence on the host states is difficult. First, it is important to note that whether the influence is negative or positive differs from instance to instance and according to the criteria used for evaluating the influence. Is an MNC's impact to be judged from an economic or environmental point of view? In addition, bargaining power between MNCs and host states, which is the key to controlling outcomes positive or negative, changes over time.[52] The balance of bargaining power between a particular MNC and the host government is subject to change over time, and collective bargaining power between MNCs and host states is subject to change by developments of the international political economy. The bargaining power of oil producing developing states, for instance, rose against the international oil majors in the OPEC oil embargo and remained strong for several years after the embargo.

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[50] Peter Evans, Dependent Development: the Alliance of Multinational, State, and Local Capital in Brazil, (Princeton: Princeton University Press, 1979).

[51] Raymond Vernon, Sovereignty at Bay, (New York: Basic Book, 1971).

Therefore, it is difficult to draw generalizations about the influence of Japanese MNCs over the host states. There is also a paucity of scholarly works on the topic due to the quite recent expansion of Japanese MNCs in the international political economy. In addition, it is not necessary to make generalizations concerning host states in this thesis. For this thesis studies Japanese FDI, the main activity of Japanese MNCs, with most emphasis on the supportive relationship with the Japanese government, rather than the relationship between Japanese MNCs and host states except the case with Daishowa. The possible shortcomings of not generalizing about influences here may be partly compensated for by the case study of the fifth chapter, which studies and evaluates the issues surrounding a particular case of Japanese FDI in the host state. For the further study of the relationships, reference books are noted in the footnote.[53]

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[52] Theodore H. Moran, Multinational Corporations and the Politics of Dependence, (Princeton: Princeton University Press, 1974), 159-160.

## Conclusion

This chapter reviewed the applicability of established theories of FDI based on studies of Western MNCs to Japanese FDI after the Second World War, and supplemental theories to explain Japanese FDI. The product cycle theory does not recognize Japanese multinational manufacturing corporations as "followers" of the Western product-innovators.[54] The industrial organization theory does not explain why the Japanese small- and medium-sized MNCs were able to make FDI, despite the lack of firm-specific advantages because their shortcomings were compensated by the Sogoshosha and the economic-nationalist Japanese government. However, this theory does explain the FDI made by the oligopolistic Japanese industrial manufacturers in the United States and Western European states.

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[53] The positive influence, Kiyoshi Kojima, Nihon no Kaigai Chokusetsutoshi (Japanese Foreign Direct Investment); Toshio Shishido and Mitsuhiko Yamada, Shin Nihon Kigyo in USA (New Review: Japanese Enterprises in the U.S.A), (Tokyo: Toyo Keizai Shinpo Sha, 1988), the negative influence, in the United States, Martin Tolchin and Susan Tolchin, Buying Into America: How Foreign Money Is Changing the Face of Our Nation, (New York: Times Books, 1988); in Australia, Takeshi Mori, "Goshuu Keizai to Nihon no Chokusetsutoshi(The Australian Economy and the Japanese Foreign Direct Investment)," in Sueo Sekiguchi, ed., Kantaiheiyoken to Nihon no Chokusetsutoshi (The Pacific Rim and the Japanese Foreign Direct Investment), in Asia, Tran Van Tho, "Nihon no ASEAN Shokoku eno Chokusetsutoshi: Seizogyo Toshi(The Japanese Foreign Direct Investment in the ASEAN States: Manufacturing Industries)," in Sekiguchi, ed., in Asia about the environmental issues, Nihon Bengoshi Rengokai(the Japan Bar Association), Nihon no Kogai Yushutsu to Kankyo Hakai: Tonan Ajia ni Okeru Kigyo Shinshutsu to ODA (Export of Pollution and Environmental Destruction: Business Expansion of Japanese Corporations in the Southeast Asia and the ODA), (Tokyo: Nihon Hyoron Sha, 1991); general evaluation, Terutomo Ozawa, Multinationalism: Japanese Style, in the United States, The Annals of the American Academy of Political Science and Sociology, 513 (January 1991).

Kojima's theory that Japanese FDI increased trade between Japan and the host states[55] was only applicable to Japanese FDI made in developing Asian states. Kojima's normative theory holds that FDI should play a role as a tutor to foster the economies of the host states. While Kojima maintains that Japanese FDI played such a role,[56] it was difficult to substantiate that the Japanese investors had the normative intention.

The theory which emphasizes changes of comparative advantage as promotive factors for increases in FDI fits Japanese FDI by different industries and different times. The changes emerged in the high economic growth led by the nationalistic government and were interpreted as scarcities which national economies will necessarily face in periods of rapid growth.[57]

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[54] Ozawa, 50.

[55] Ibid., 15.

[56] Kojima, Nihon no Kaigai Chokusetsutoshi(Japanese Foreign Direct Investment), I.

It was maintained that industrial pollution during economic growth resulted in pollution-causing industries making FDI because they faced public opposition and tightened governmental regulations.

This chapter also argued that relationship between Japanese MNCs and their government is both similar to and different from the U.S. analogous relationships. They were similar in the firm accord of the two parties' interests in securing raw materials, earning foreign exchange reserve and maintaining economic status; they were different in government's efforts to use the MNCs as tools securing raw material for military purposes, propagating the ideology of the free-market economy, and conducting favorable diplomacy.

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[57] Ozawa, 66.

# CHAPTER THREE: Japanese Foreign Direct Investment Historical Development and Issues

## Introduction

This chapter will examine the historical development of Japanese foreign direct investment (FDI) after World War II, and demonstrate how international (as opposed to domestic) factors have become increasingly important determinants of FDI since the 1970s. It will contend that the Japanese government took advantage of Japanese FDI in order to shape the national economy according to its own designs. A study of Japanese FDI in resource-related industries will attempt to substantiate this thesis. Since large Japanese trading companies have been deeply involved in the expansion of Japanese FDI, their role will be also studied.

## Brief Review of the Historical Development

The influence of domestic factors on FDI was, in the early post-war years, much greater than that of international factors. The reason for this is that Japan, a "capitalist developmental state"[1], avoided unfavorable international influences on its economy by setting regulatory foreign economic policies in the relatively stable international economic system maintained by the U.S. hegemon. However, since the early 1970s, economic and political changes in the international sphere have been increasingly affecting Japanese FDI. Why? First, the hegemonic economic status of the United States has been declining; and second, economic interdependence[2] among states has been increasing. Consequently, each state has become more vulnerable to changes in other national economies and the international economy. In addition, because of the above two developments, international trade has become increasingly politicized. Meantime, since its economy has become more significant to, and integrated with, the international economy, Japan, like other developed states, has continued to deregulate its laws affecting cross-border economic activities, including FDI. It should be noted that there has been pressure on Japan to deregulate from the major industrialized states, especially the United States.

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[1] Chalmers Johnson, MITI and the Japanese Miracle: The Growth of Industrial Policy, 1925-1975, (Tokyo: Charles E. Tuttle Co., 1982), VIII.

Unchanged features of FDI are: small- and medium-sized firms have been making more FDI than large-sized firms;

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[2] The definition of "economic interdependence" in this paper is "the fact or condition of depending each upon the other; mutual dependence" in economy. Richard Cooper, "Economic Interdependence and Coordination of Economic Policies" in Jones and Kenen, eds., Handbook of International Economics 2 Vols. (Amsterdam: North-Holland. Kahler, Miles, 1985), Vol. 2, 1196 quoted in Robert Gilpin, The Political Economy of International Relations, (New Jersey: Princeton University Press, 1987), 17; the "interdependence" is "mutually albeit not equal dependence," however, "the concept of market or economic interdependence is a highly ambiguous term." Gilpin, 17-18.

collective investments (i.e., minority share-holdings[3]) have been most active; the large general trading companies(Sogoshosha) have been playing promotive roles in the increases of FDI.[4] But since the mid-1970s, the amount of FDI in the form of majority share-holding by large, oligopolistic Japanese firms has increased. This trend is backed by the high availability of funds to the oligopolists, and is the preferred means of those firms looking to increase their control over FDI. Until the first half of the 1980s[5], the largest portion of Japanese FDI went to developing nations.[6] However, the total amount of FDI in Western industrialized states has exceeded that in the developing nations since 1984.[7] But since the mid-1970s, the amount of FDI in the form of majority share-holding by large, oligopolist Japanese firms has increased. This trend is backed by the high availability of funds to the oligopolists, and is the preferred means of those firms looking to increase their control over FDI. The main purposes of FDI until the mid 1970s had been those of securing raw materials for heavy industry, using cheap labor in developing countries, and transferring heavy and chemical industries abroad. An important new purpose since the mid-1970s has been circumventing and even neutralizing trade friction between the Western industrialized states. The large trade imbalances between Japan and these states became politicized during this period, and various protectionist policies were implemented in the West.

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[3] Two or three firms make one FDI together by sharing the total capital necessary for the FDI. Large trading companies have often participated in this type of FDI and helped the other participant firms in various way. For a detailed study of the role of the trading companies, see the section about trading companies in this chapter.

[4] Kiyoshi Kojima, Nihon no Kaigai Chokusetsutoshi (Japanese Foreign Direct Investment), (Tokyo: Bunshindo, 1987), 22.

[5] Although international factors had started to influence Japanese FDI in the early 1970s, the result of the influences actually appeared in the mid-1970s in the changes in the growth, the regional and the industrial compositions of the FDI, i.e., the aspects influenced by domestic factors in the previous years continued to be so influenced until the mid-1970s.

[6] The Economic Planning Agency, Keizai Hakusho Showa 63 Nendo (Economy White Paper 1989); (Tokyo: Ministry of Finance, 1989) 471. Kojima, 4, 22.

[7] Ibid., 471.

The "product cycle theory" was applicable to most Japanese FDI before the mid-1970s at the point that we can find differences of comparative advantage among national economies.[8] Since then, Krugman's "industrial organization theory of vertical integration," which emphasizes aspects of MNC business strategies, has been more applicable to the new developments.[9]

## The Industrial Policy

Chalmers Johnson writes: "In states that were late to industrialize, the state itself led the industrialization drive, that is, it took on developmental function."[10] Indeed, Japanese industrial policy created rapid economic growth in the post-war era and had great influence over the development of Japanese FDI. For this reason, and in order to show the basic attitude of Japanese business toward the industrial policy (including the regulation of FDI), the industrial policy of the high-growth era will be studied briefly.

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[8] Gilpin, 234-236.

[9] Ibid., 234-235.

The Ministry of International Trade and Industry (MITI) played a central role in industrial policy. It designated as "targeted industries" those industries which were thought to encourage economic growth and to increase Japanese exports, and provided them with subsidies, special tax treatments and infrastructure.[11] In the 1950s and 1960s, heavy and chemical industries were the "target industries." Led by these industries, the Japanese economy quickly recovered from the devastation of the war and grew at an historical rate.[12] The government adopted import restrictions to protect and foster domestic industries, but promoted the import of technologies useful for economic growth. It expertly used financial systems as the most important tool of its industrial policy.

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[10] Johnson, 19.

[11] Ibid., 211, 218.

[12] In the 1960s, the average annual growth of the Japanese gross national product (GNP) was 11.6 percent and that of export was 16.8 percent. Hiroshi Takeuchi, Showa Keizai Shi (History of the Economy in the Showa Era), (Tokyo: Chikuma Shobo, 1988), 162.

Low interest-rate policies and government financial institutions contributed significantly to economic growth.[13] The MITI even made business plans for industries and carried out "administrative guidance" to promote their efficient growth.

The government strictly controlled the cross-boarder flow of capital to enhance the effectiveness of industrial policy as well as to accumulate[14] foreign exchange received from exports. Laws controlling the flow of capital were the Foreign Exchange and Foreign Trade Control Law (FEFTCL) enacted in 1949 and the Foreign Capital Law (FCL) of 1950. The FEFTCL, the law regulating Japanese FDI, has been gradually deregulated as the FDI has increased. The FCL regulated inward FDI to Japan.

Japanese business cooperated with the government because of its appropriate interventions[15] in the market and the government's generally favorable support. The "corporatism" of this era reflected the "responsive dependence"[16] of business and a strong economic nationalist government on each other, but the underlying common interest of the two, and perhaps the interest of the people as well, was the imperative of developing the economy to improve terrible living conditions after the war.[17]

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[13] Johnson, 209, 211, 217, 237. Takeuchi, 203.

[14] Ibid., 217.

[15] Ibid., 29.

[16] Gary D. Allinson, Japanese Urbanism: Industry and Politics in Kariya, 1872-1972, (Berkeley: University of California Press, 1975), 43-45, quoted in Johnson, 24.

## Historical Development of Japanese FDI

Following Terutomo Ozawa's division of the historical development of Japanese FDI,[18] the periods (1) 1951 to 1967, (2) 1968 to the oil embargo in 1973, (3) from the oil embargo to the mid-1980s, and (4) the late 1980s, will be studied.

### (1) From 1951 to 1967

During the early 1950s, the average annual new FDI in Japan was "less than 10 million dollars."[19] This was due to the country's small foreign exchange reserve[20] and the insufficient recovery of Japanese firms after the war. The annual new FDI increased gradually. In 1966, the approved amount of FDI reached US $20 million.[21]

The United States was the largest recipient of Japanese FDI during the 1950s (see APPENDIX 1).[22] The main purpose of this FDI was to re-establish the trading companies' and manufacturers' sales branches to promote export from Japan.[23]

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[17] Johnson, 196-197.

[18] Terutomo Ozawa, Multinationalism, Japanese Style, (New Jersey: Princeton University Press, 1979), 11-12.

[19] Ibid., 13.

[20] Ibid., 13.

[21] Ibid., 14.

[22] Ryutaro Komiya and Ryuhei Wakasugi, "Japan's Foreign Direct Investment," The Annals of the American Academy of Political Science and Sociology, 513 (January 1991): 52, Table 1.

The FEFTCL required time- and labor-consuming procedures from Japanese firms when they made FDI, but did not seem to be pose an inconvenience for these firms since they did not consider going beyond the regulations to make large-scale use of FDI. During this period the government viewed FDI as a means to promote Japanese export and secure raw materials for industry. FDI was not intended to affect the sound domestic operation of Japanese firms or the government's monetary policy.[24]

The trade policy of foreign states is one of the determinants of FDI. Japanese manufacturers made FDI in Brazil, Mexico and Argentina in the late 1950s and early 1960s, to sell their goods in the local markets since the host governments implemented policies of import substitution. However, in the early 1960s the economic and political environments for FDI in these countries deteriorated through growing inflation and nationalism. Consequently the growth of Japanese FDI stagnated.[25]

### (2) From 1968 to the Oil Embargo in 1973

Japanese FDI recorded "phenomenal acceleration" (see APPENDIX 2)[26] during the period from the late 1960s to 1973;

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[23] Ozawa, 11-12.

[24] Ibid., 13.

[25] Ibid., 13.

[26] Ibid., 11.

in 1968, the amount of annual new FDI doubled to US $557 million from that in 1967.[27] The reason for the acceleration was the increase in Japan's foreign reserves[28] from exports of heavy and chemical industries fostered by the industrial policy.[29] The accumulated foreign reserve needed places to be invested. However, investment in Japanese industry reached saturation point in the late 1960s. Consequently, the foreign reserve was used for FDI. Responding to the rapid increase in available capital for investment, the government simplified the procedures for authorization of FDI and raised the legal limit of investment.[30] These deregulations caused further increases in FDI.

The adoption of the floating foreign exchange rate system in February 1973 resulted in the relative decline of the United States' status in the international economy, and raised the comparative value of the yen to the U.S. dollar by 35 percent in the same year.[31] Market expectations of another increase in the yen's worth[32] and Japan's large foreign exchange reserve,[33] pushed the value of the yen higher still. In order to curtail the yen's growth, the government promoted imports and FDI.[34] As a result, Japanese FDI continued to grow.

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[27] ibid., 15.

[28] Ibid., 16.

[29] The trade surplus was increased from US $2.5 billion in 1968 to US $7.8 billion in 1971. Ibid., 15.

[30] The earlier "case-by-case" examination by the Ministry of Finance changed in 1969 into "automatic approval" for FDI of less than US $200,000 from the Bank of Japan, and the ceiling was raised to US $1 million in next year. Ibid., 16-17.

[31] Ibid., 16.

[32] Ibid., 16.

### Rapid Growth of FDI in Asia and its Consequences

The amount of Japanese FDI in Asia increased rapidly in this period[35]; from 1968 to 1971, the cumulative amount of FDI increased by two times that of the previous sixteen years.[36] The main recipients of the new FDI were labor-intensive manufacturing industries -- particularly the textile industry. The reasons for the increases were: rapid growth of workers' wages made possible by a burgeoning economy,[37] the shortage of younger Japanese workers,[38] and the host governments' policies for promoting FDI (such as tax credits).[39] The cumulative amount of Japanese FDI in Asia became the largest portion of the cumulative amount of all Japanese FDI by the end of 1973.[40] The FDI in manufacturing industries in Asia continued to increase to 51.4 percent of all Japanese FDI in 1973.[41] The Asian governments' additional incentives to FDI contributed to the increase.[42] The international trade environment further promoted Japanese FDI. Preferential treatment of exports from the so-called less-developed countries (LDCs) allowed Japanese manufacturers to enjoy lower tariffs on exports from the LDCs to industrialized states.[43] The Japanese textile industry bypassed the "voluntary export restraint" imposed by the United States in 1971.[44]

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[33] It reached the "record high" level of about US $19 billion in February 1973. Ibid., 16.

[34] To promote FDI, the government facilitated lower interest-rate loans, longer-term funds in foreign currencies and tax-exemptions on Japanese firms' loss reserves for their FDI. Sueo Sekiguchi, "Nihon no ASEAN Shokoku eno Chokusetsutoshi: Shigen Kaihatsu Toshi (Japanese Foreign Direct Investment in the ASEAN Countries: Developmental Investment in Resources)" in Sueo Sekiguchi ed. Kantaiheiyoken to Nihon no Chokusetsutoshi(The Pacific Rim and The Japanese Foreign Direct Investment, (Tokyo: Nihon Keizai Kenkyu Center, 1982), 61.

[35] Sueo Sekiguchi, "Preface," in Sueo Sekiguchi, Ibid., 10.

[36] Kojima, Nihon no Kaigai Chokusetsutoshi (Japanese Foreign Direct Investment, 89.

[37] Japanese workers' annual wages were increased by about 15 percent per year from the late 1960s to the early 1970s, Komiya and Wakasugi, 51.

[38] Ozawa, 14.

Along with increases in FDI, strong anti-Japanese sentiment grew among some Asian peoples. Such sentiment took the form of anti-Japanese riots and demonstrations in Thailand and Malaysia when prime minister Tanaka visited those countries in 1974.[45] To respond to this problem, Japanese investors instituted codes of conduct. The host governments revised their policies regarding FDI. They set limits on foreign share-holdings, made provisions for favourable treatment of foreign capital more selective, and imposed on foreign investors the obligation of hiring indigenous ethnic groups. As a result, the anti-Japanese sentiments abated somewhat.[46] Although the Japanese government started to reconsider Japan's relations with Asian states, its response to the incidents was rather slow.[47]

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[39] Thailand adopted such a policy in 1962, the Philippines and Korea in 1965, Indonesia and Singapore in 1967 and Malaysia in 1968. Ozawa, 16; Tran Van Tho, "Nihon no ASEAN Shokoku eno Chokusetsutoshi: Seizogyo(The Japanese Foreign Direct Investment in the ASEAN States: Manufacture Industries)", in Sekiguchi, ed., 28.

[40] The ratio was 24.3 percent. Kojima, 90.

[41] Ibid., 97.

[42] The purpose of the incentives was export promotion from the states. Malaysia created the Free Trade Zone in 1971, the Philippines the Export Processing Area in 1972. Tho, 28.

[43] Tho, 29; The treatment had been first adopted by the United States and other industrialized states in the early 1970s and became a rule of the GATT as the Generalized Systems of Preferences (GSP) at the Tokyo Round talks, Gilpin, 196.

[44] Ibid., 29.

A domestic problem caused by the high economic growth also contributed to an increase in FDI. In this period, it became difficult for heavy and chemical industry to expand operations in Japan. Many areas along coastlines suitable to such operations had already been developed as designated industrial zones for these industries during the 1960s.

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[45] The reasons for anti-Japanese sentiments included increased economic nationalism caused by too-rapid introduction of Japanese FDI, the increase in the disparity of wealth by Japanese FDI, and the strong Japanese business ties with the so-called "overseas Chinese" in the states, in spite of anti-overseas-Chinese sentiment in the indigenous ethnic groups in these societies. See Tho, 34.

[46] Ibid., 31.

[47] Three years after the riots, the Fukuda government adopted the "Manila Doctrine" emphasizing Japanese economic cooperation in South East Asia.

Furthermore, the expansion was opposed by residents in the proposed areas because of tremendous environmental damage caused by these industries during the high-growth period: one characterized by lenient environmental regulations of the national and local governments. Citizens suffering from the pollution indicted industry and governments. Consequently, governments tightened environmental regulations and industry had to bear the huge cost of pollution-controlling devices. This made domestic expansion less favorable for them.

The MITI was accused of haphazard promotion of high industrial growth and "appalling bureaucratic apathy toward the pollution problem."[48] Finally, in 1971 the MITI advocated a structural shift of Japanese industry from its emphasis on heavy and chemical industries to an emphasis on knowledge-intensive industries which would not cause these problems.[49] Since Japan is a "capitalist developmental state,"[50] the goals of its industrial policy are accomplished by explicitly and implicitly institutionalized measures. Thus, the heavy and chemical industries gave up domestic expansion and made FDI in resource-producing states or in states where environmental regulations were less strict than in Japan.

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[48] Johnson, 289.

[49] Ibid., 290; Ozawa, 19. The government also advocated that resource-consuming industries should operate in the resource-producing states. This reflected the government's concerns over the increasing import of raw material in the late 1960s, i.e., increasing dependency of the economy on other states and/or MNCs.

[50] Johnson, VIII.

(3) From the Oil Embargo to the Middle of 1980s

Since the early 1970s, international economic and political factors have affected Japanese FDI more than domestic factors have. In response to acute anxiety over resource-scarcity, Japanese FDI aimed at securing raw materials increased rapidly. But this impetus stagnated in the recession that followed the oil crisis of the 1970s, with a reduction in resource consumption by the "untiring efforts"[51] of Japan's energy-consumption industries and a rise in wages in Asian states.[52] Thus, as a whole, the growth of Japanese FDI slowed down between 1973 and 1980.[53] After 1980, growth accelerated again (see APPENDIX 2). In this period, FDI increased in response to the politicization of international trade.[54]

Japanese firms began to finance their FDI in the international money market that expanded rapidly after the adoption of the floating rate system.[55] Affluent "oil dollars" made financial conditions favorable for them.

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[51] The energy consumption per unit output decreased "by between 10% and 20%, oil consumption by between 15% and 70%." Nobutoshi Akao, "Resource and Japan's Security" in Nobutoshi Akao ed., Japan's Economic Security: Resource as a Factor in Foreign Policy, (Hampshire: Biddles Ltd., 1983), 35.

[52] Komiya and Wakasugi, 54.

[53] Ibid., 54; Kojima, 89.

[54] Manufacture industries received the largest portion of the FDI in this period. Komiya and Wakasugi, 54.

In 1980, the Japanese government totally revised the FEFTCL to permit, in principle, all foreign exchange transactions. This was merely the recognition of the *de facto* financial activities of Japanese firms and financial institutions, of their FDI and foreign portfolio investment.

### Development and Import

The two oil crises inflicted huge damage to the Japanese economy because of Japan's heavy dependency on oil from the Middle East. How Japan dealt with the scarcity of not only oil but also other natural resources, how it tackled the two oil crises, and the impact of these measures on its FDI will be studied in this section and the next section.

In a market economy, a state's "specialization and its resulting dependencies increase vulnerabilities to untoward events."[56] Japan's resource scarcity had been exacerbated by Japan itself; it had increased its demand for raw materials in the 1960s by state-led high economic growth emphasizing the resource-consuming industries.[57]

In the 1950s Japan had supplied itself with raw materials in spot-purchases from the international majors because the demand had not been significant compared with the total supply in the world market.[58] The demand escalated from the mid-1960s, and Japan became the world's largest importer of certain raw materials; in 1969 the ratios of Japan's imports to the total world trade of oil, iron ore and timber were 15.6, 39.3 and 29.9 percent respectively.[59] Along with these increases, Japan's resource-consuming industries had come to be troubled with unstable supplies from the majors, with cancellations and delays. Thus securing more stable supplies became an increasingly critical issue for the industries and a government concerned with the dependency of the Japanese economy on overseas resources.

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[55] Ozawa, 18.

[56] Gilpin, 23.

[57] For the reasons for the government designation of the resource-consuming industries, see the section on the historical development of Japanese FDI in this chapter.

In the late 1960s, Japanese firms started to adopt so-called "Development and Import" (D & I) in their FDI to secure raw materials in developing states. D & I entails that Japanese firms "help develop food-stuffs and natural resources abroad for guaranteed exports to Japan."[60] According to Ozawa, the approach of D & I needs more "skills" than simple importation because it "involves direct, although partial, participation in the ownership and extraction of resources in the host country."[61] The local partners include private firms and governments.[62] This is a good way to deal with the resource-nationalism of producing states (including the desire to maximize rents from natural resource development with/by foreign investors[63]), which quickly escalated after the oil embargo. D & I attempts to assist the host states, but it is "an implicit condition" for foreign investors to assist the economic development of the developing, resource-producing states when these investors need the natural resources.[64] D & I increased rapidly from 1968 to 1970,[65] especially in Southeast Asia and Latin America.[66]

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[58] Kiyoshi Kojima, "Japan's Resource Security and Foreign Investment in the Pacific: A Case Study of Bilateral Devices between Advanced Countries," in Lawrence B. Krause and Hugh Patrick, eds., Mineral Resources in the Pacific Area, papers and proceedings of the Ninth Pacific Trade and Development Conference held in San Francisco, Cal. Aug. 22-26. (California: Federal Reserve Bank of San Francisco, 1977), 507.

[59] Ozawa, 160.

[60] Yoshi Tsurumi, Japanese are Coming: A Multinational Interaction of Firms and Politics, (Massachusetts: Ballinger Publishing Co., 1976), 55.

The Japanese government encouraged Japanese firms to increase D & I by providing opportunities, funds and technical assistance through its provision of ODA, as well as tax exemptions for losses resulting from D & I in the developing states and the FDI in resource industries.[67]

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[61] Ozawa, 183.

[62] Ibid., 184.

[63] Sekiguchi, 56.

[64] Ozawa, 184.

[65] Ibid., 170.

[66] Kojima, 125.

[67] Sekiguchi, 61.

## The Oil Crises and FDI

The economic interdependence which grew from the 1960s has increased the vulnerability of individual states to changes in other national and international economies. The effect of such changes on a national economy varies according to the vulnerability of the state. Although the MITI advocated that Japan's leading industries should go from the resource-consuming heavy and chemical industries to the less resource-consuming and more knowledge-intensive industries in 1971, the time before the oil embargo in 1973 was too short for the economy to make such a transition. The oil embargo affected the Japanese economy significantly because of the country's increased vulnerability to shortages of raw materials. The embargo raised energy costs and caused inflation. The resource-nationalism of resource-producing states, the growth of international commodity cartels and the nationalization of the international majors--all triggered by the oil embargo--strengthened the bargaining power of the resource-producing states against the MNCs and consumer-states such as Japan. These conditions had a huge impact on Japanese FDI in resource-related industries and the Japanese government and people became acutely aware of their country's vulnerable status.

States strive to "enhance their own independence " in the "hierarchical, dependency, and power relationship among groups and national societies" brought on by advancing economic interdependence.[68] Facing the oil crisis, the economic-nationalist Japanese government further devoted itself to securing a stable supply of oil and other raw materials. It adopted its so-called "oil diplomacy" immediately after the oil embargo in 1973,[69] and succeeded in increasing the direct purchases of oil from the producing states in the Middle East, which were regarded as a more stable source of supply than the purchases from the oil majors.[70] In order to increase direct purchases, the government was quick to provide Official Development Assistance (ODA) to the region.[71]

While coping with the immediate crisis, the government also had to reconsider its entire policy of securing raw materials, and introduced new policies. ODA provisions to resource-producing states were increased in order to foster closer ties. The provisions often took the form of a mega-project in resource-related industries and created opportunities for Japanese firms to make FDI. As a result, they reinforced the stable supply of raw materials through "Japanese hands" from the producer-states. A law was enacted in 1975 to maintain an oil stockpile sufficient for 90 days.[72] Policies for the promotion of FDI in resource-related industries -- such as tax-exemptions from the loss reserve in FDI[73] -- were also adopted. The government encouraged the conservation efforts of Japanese firms[74] and promoted public and private research and development for alternative sources of energy. It made further efforts to promote the structural shift of Japanese industry from resource-consuming to knowledge-intensive.

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[68] Gilpin, 23.

[69] The government sent successive envoys of high-ranked government officials to the Middle East. Ozawa, 144. It also shifted from its pro-Israel policy -- in which it had taken after the United State's Middle East policy -- to a pro-Arab approach.

[70] This was because the oil majors discriminately stopped their oil supply to Japan when the OPEC state started to reduce their oil production during the first oil crisis. The supply through the oil majors was 70 percent of Japan's total oil imports in 1976 and decreased to 43 percent in 1980, Akao, 23.

[71] The amount of the loans and the ODAs granted to the Middle East reached to five times of the amount of those granted in 1972. Ozawa, 144.

As a result, Japanese FDI in resource-related industries in the resource-producing countries grew rapidly, especially in the Middle East.[75] Nevertheless the government wanted to reduce the total capital outflow because of trade deficits which followed price hikes in oil.[76]

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[72] In 1973, the stockpile was only to last 49 days, Teruyasu Murakami, "The Remarkable Adaptation of Japan's Economy" in Daniel Yergin and Martin Hillenbrand, eds., Global Insecurity: A Strategy for Energy and Economic Renewal, (Massachusetts: Houghton Mifflin Company, 1982), 146.

[73] The government used public corporations in support of FDI to secure raw materials. The Metal Mining Agency and the Japan Petroleum Development Corporation have supported FDI of the respective constituencies. Philip Crowson, "Non-fuel Mineral Procurement Policies" in Akao, 145; Michael Y. Yoshino, Japan's Multinational Enterprises, (Massachusetts: Harvard University Press, 1976), 53.

[74] Energy-consuming industries reduced energy consumption per unit output "by between 10% and 20%" and the "oil consumption by between 15% and 70%" during the period from 1973 to 1979, in Akao, 35.

[75] Ozawa, 19; The Japanese oil industry, in cooperation with the government, increased FDI in Brazil, China and so forth. However, in terms of their scales and exports to Japan, they have not been significant compared with those in the Middle

Further promotion of the structural shift of Japanese industry was reflected in the changes made to the industrial composition of Japanese FDI in Asia. Instead of labor-intensive light manufacturing industries, intermediate-goods manufacturing ones such as pulp-making, lumber and nonferrous metal smelting received the largest portion of available FDI.[77] FDI in resource-consuming and/or polluter industries sought to exploit cheaper energy costs and to expand operations which had become difficult in Japan.[78] Tariffs were cut to promote the import of intermediate goods manufactured in Japanese FDI.[79]

However, soon thereafter, the "era of low economic growth" inaugurated by the oil crisis slowed the expansion of

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East.

[76] The government actually restricted the outflow by administrative guidance. But it could not stop the impetus of the flow; the decline of new investment in 1974 was only a reflection of the recession caused by the oil crisis. Ibid, 19.

[77] Kojima, 97.

[78] The difficultly of domestic expansion of these industries explained earlier in this chapter was another factor promoting FDI. A good example of the structural changes is the aluminum refiners' case; the MITI made them deinvest and arranged a mega-ODA project in Indonesia for their D & I in order to increase the import of aluminum products from "Japanese" refiners. Edward J. Lincoln, Japanese Unequal Trade, (Washington D.C.: The Brookings Institution, 1990), 110.

[79] Ibid., 110.

demand for raw materials. In addition, the success of Japan's industrial energy conservation, and the advancement of structural changes to Japanese industry, made foreign investments in resource-related industries less urgent.

As a result, the consequences of the oil crisis of 1979 were less serious for Japan than the first oil crisis. The measures taken by the government and the Japanese industries emphasized conservation efforts and the development of alternative sources of energy. Interestingly, this second oil crisis ultimately produced changes favorable to Japan.[80] The importance of the OPEC states in oil supply continued to decrease after the recession started in 1981; market- and short-term sales replaced "government-to-government" sales. Japan's FDI reinforced the decreases in the importance --Japan invested in numerous areas of potential oil supply, creating competition among the oil producing states. As a result, it became easier for Japan to secure its oil supply.

In the mid-1980s, the government's task of securing raw materials became easier, and the growth of Japanese FDI in resource-related industries was slowed even more by further changes in the international economy. These changes included declines in prices of raw materials, including oil (the market-price of which went down to about one third of its peak level in 1981[81]), and the rapid appreciation of the yen. Energy-conservation efforts initiated by Japanese industry[82] further lightened the government's burden, as well as the onus on those making FDI in resource-related industries.

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[80] Murakami, 159.

Trade Frictions and FDI

The continuing growth of the yen after December 1975, had, by October 1978[83], made the price of foreign assets much cheaper, and forced Japanese exporters to take measures to avoid foreign exchange risks by making FDI.[84] However, the most important factor in the promotion of their FDI was the so-called new protectionism. Industrialized states such as the United States and Western European states adopted protectionist trade policies such as "voluntary export restraints" against Japanese exports of automobiles, steel, electrical apparatus and so forth. Furthermore, charges of dumping were leveled against the exporters to these two regions. To avoid trade frictions as well as to continue to sell their products, the Japanese manufacturers, most of whom were powerful oligopolies, made FDI in the regions in the form of majority share-holdings.[85] The United States and Canada had received a total of US $303 million in FDI from 1951 to 1972; however, the cumulative amount of FDI in the United States alone had reached US $16.5 billion by 1984.[86] New FDI in European states in 1975 was US $333 million and in 1984 it had reached a total of US $1.937 billion. As a result, the United States and Europe received more than half of the new Japanese FDI in 1984 (see APPENDIX 3).[87] Since their operations were capital-intensive, their FDI increased the total amount of all FDI in manufacturing industries.

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[81] Jun Nishikawa, Sekai Keizai Nyumon (World Economy: A Guide), (Tokyo: Iwanami Shoten, 1991), 67, Figure 4-3.

[82] Japanese import of oil decreased from a peak of about 320 million kiloliter in 1973 to 250 million kiloliter in 1986. Although it increased to 290 million kiloliter during the boom-year of 1989, Nishikawa, 106; the consumption per unit output of the GNP in 1989 was 64.5 percent of that in 1973, the Economic Planing Agency, "Keizai Hakusho Heisei 3 (Economy White Paper 1991)," Ekonomisuto(special issue) (August 1991):276.

[83] The value of the yen rose by 35% during the period. See Nishikawa, 63, Figure 4-2.

[84] Ozawa, 20-21.

To these forms of FDI, the "industrial organization theory of vertical integration" was applicable. The theory maintains that "the production of output in some plants... serve(s) as input for other plants of the firm."[88] About 70 percent of the parts and components used in overseas production were imported from Japan.[89] This, and the large scale of this type of FDI, meant that the oligopolist manufacturers that made FDI would be "full-fledged multinational corporations."[90]

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[85] Kojima, 105, Table 3-6.

[86] Kiyohiko Fukushima, "Japan's Real Trade Policy," Foreign Policy, no. 59 (1985): 23-24 quoted in Gilpin, 259.

[87] the Ministry of Finance, 471, No.2-2-14-3.

[88] Gilpin, 235.

[89] Terutomo Ozawa, "Japanese Policy Toward Foreign Multinationals: Implications for Trade and Competitiveness" in Fragile Interdependence: Economic Issues in U.S.-Japan Trade and Investment,ed., Thomas A. Paugel (Massachusetts: Lexington Books, 1986 ), 142-162 quoted in Bela Balassa and Marcus Noland, Japan in the World Economy, (Washinghton D.C.:

## (4) The Late 1980S

In the later half of the 1980s, the growth of Japanese FDI suddenly accelerated. From 1980 to 1985, the average annual outflow of FDI was about US $8.6 billion, but the outflow in 1986 was about US $22.3 billion, and in 1989 it had reached US $60 billion. As a result, the total outflow in three years alone, from 1986 to 1989, had surpassed all FDI up to 1986.[91] Finally, FDI had become an important activity in Japan's national economy. FDI recorded 1.2 percent of the gross national product in 1988; comparable figures for the United Kingdom, the United States and West Germany were 3.7 percent, 0.4 percent and 0.8 percent respectively.[92]

In this period, the factor which most affected the increase in Japanese FDI was the dramatic rise in the value of the yen against the U.S. dollar. This change resulted from policy coordination among the "Group of Five" (G5) states following the Plaza agreement of 1985.[93] Policy coordination

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Institute for International Economy, 1988), 14.

[90] Komiya and Wakasugi, 61.

[91] Ibid., 54.

[92] Ibid., 54-55.

[93] The G5 states are Japan, the United States, West Germany, the United Kingdom and France. The purposes of the Plaza Agreement were to reduce the huge Japanese trade surplus

is carried out when governments recognize that "the opportunity costs of not coordinating policy increase compared with the cost of sacrificing autonomy as a consequence of making binding agreements."[94] The value of the yen went up by about 60 percent in just one year.[95] Consequently, the value of foreign assets for Japanese investors was cut by more than half, and Japanese FDI increased.[96] Another international factor in the promotion of FDI was the planned European Community integration in 1992. Since this integration was perceived by Japanese manufactures as a serious potential hindrance to their exports to Europe, but Europe nevertheless was a prospective growing market for their products, they made FDI in Western Europe to secure a foothold for sales. Enthusiastic invitations to Japanese FDI from national and local governments in North America and Western Europe who were willing to create promotional policies also

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against the United States, which reached US $33 billion in 1984, as well as the entire Japanese trade surplus and the entire American trade deficit, which were US $44.2 billion and US $112.7 billion respectively in 1984. Yoshikazu Miyazaki, Sekai Keizai wo Dou Miruka (A View about the World Economy), (Tokyo: Iwanami Shoten, 1986), 171-173; Masahiro Kawai and Motoshige Itoh, Kokusai Keizaigaku Nyumon (A Guide to the International Economy), (Tokyo: JICC, 1991), 32.

[94] Robert O. Keohane, "Multilateralism: an agenda for research," International Journal, XIV, (Autumn 1990): 742.

[95] Nishikawa, 64.

[96] A study of the Bank of Tokyo shows that the newly increased Japanese FDI reduced the surplus to some extent, "Growth of Overseas Direct Investment and Its Impact on the Balance of Trade," Tokyo Financial Review Bank of Tokyo, Vol. 16, No. 8, (August 1991), 5-6.

increased FDI.[97]

The shift from the developing states to the Western developed states as recipients of Japan's FDI continued. About two thirds of the FDI between 1986 and 1988 went to North America and Western Europe (see APPENDIX 1).[98] The former characteristics of Japanese FDI, i.e., FDI mainly in developing states, became irrelevant. The Japanese government had exerted much influence over FDI in the past, but few government policies for restricting or promoting FDI existed in the late 1980s, and they had little to do with the rapid increase of FDI in North America and Western Europe. Rather, the change was brought about by business in the interest of globalizing Japanese industry.[99]

Service industries such as finance, insurance and real estate[100] became the largest recipients of FDI; investment in these industries occupied more than 70 percent of total

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[97] Komiya and Wakasugi, 56-57; It is difficult to prove the relationship between such invitations and the increase in FDI, however, the invitations are not easily ignored as a factor in the increases in some cases. For example, a former governor of Illinois visited Japan eight times to invite Japanese FDI to the state. During his term of office, the number of Japanese factories in the state increased from 259 to 592. Some of the invitations include contradictory elements. For example, John Kerry, Massachusetts Senator and critic of the Keirestu system, is also eager to invite FDI, Gaiko Forum(Foreign Policy Forum), (November 1991), 63.

[98] Komiya and Wakasugi, 54.

[99] Ibid., 54, 56.

[100] The purpose of FDI in the real estate industry was to gain "returns" i.e., "rents and capital gains" "on the capital invested" "similar to indirect investment." Ibid., 56.

Japanese FDI.[101] Financial institutions in Japan made FDI as a response to the on-going "securitization" of finance, and as a reaction to tougher competition among them, which was caused by financial deregulation in Japan and the sluggish growth of its economy.[102]

## Investment Friction

As a result of the rapid growth of Japanese FDI in the United States and so-called "trophy deals" like the takeovers of the Rockefeller Center Building and Columbia Pictures[103], the "investment friction" between Japan and the United States has grown.[104] The origins of the friction are divided into three categories[105]: the people of the United States are insecure about rapid increases in Japanese FDI in their states; FDI has not contributed to the development of technology or the growth of U.S. industry, and has caused human-management problems;[106] Japanese institutional arrangements have "impede(d)"[107] the growth of FDI in Japan by other nations, and as a result, the amount of FDI in Japan and Japanese FDI in other countries have become asymmetrical.[108]

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[101] Ibid., 54.

[102] J. Thorsten Duser, International Strategies of Japanese Banks: the European perspective, (London: Macmilian Academic and Professional Ltd., 1990), 73-75.

[103] Kenji Yoshizawa, "Japanese Direct Investment in the U.S.," Tokyo Financial Review Bank of Tokyo, Vol. 15, No. 7 (July 1990): 3.

[104] Sylvia Ostry, Government & Corporations in a Shrinking World: Trade & Innovation Policies in The United States, Europe & Japan, (New York: Council of Foreign Relation Press, 1990), 87; The Economic Planning Agency, 318.

[105] The Economic Planning Agency, 318.

[106] Ibid., 318.

Regarding the first and second causes, the Japanese government has suggested the following measures to firms making FDI in the United States and/or in other states: they should make efforts to contribute to the local economy through their activities as well as to the host society through means such as corporate philanthropies; also, firms should be highly conscious of the legal frameworks of employment and workers' rights in the host states. These measures may work, but it will take time for their results to be clearly observed, and the observation itself will be difficult.[109]

An important consideration in the discussion of the investment "imbalance"[110] is to consider both institutional

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[107] Ostry, 87.

[108] The Economic Planning Agency, 318.

[109] The Economic Planning Agency, 320-322; The JETRO (Japan External Trade Organization), 1992 JETRO Hakusho Toshi Hen: Sekai to Nihon no Kaigai Chokusetsutoshi (1992 JETRO White Paper Volume: Investment World and Japanese Foreign Direct Investment, (Tokyo: The JETRO, 1992), 126.

[110] The ratio of the accumulated FDI "in" Japan to its GNP was lower than those ratios in the other industrialized states; the ratio in Japan was 0.3 percent and those of the United States, West Germany and the United Kingdom were 7.7, 3.0 and 14.1 percent respectively. Koji Sakurai, "Nihon no Chokusetsutoshi Gyappu" (The Gap in the Japanese Foreign Direct Investment), Asahi Shinbun (Asahi Newspaper), 8 June 1991.

(political) and economic aspects of the determinants of FDI -- economic feasibility is one of the most important determinants. A strong yen, rising fixed costs such as land prices and wages and salaries have been discouraging the increases of FDI in Japan since the mid-1980s.[111]

The most important implication of criticism of Japanese institutional arrangements is that the political decisions of the Japanese and U.S. governments influence and even alter them. Policy coordination between the two governments had already been made regarding trade issues. The coordination included measures to improve the problematic institutional arrangements against inward FDI to Japan, as impediments to the growth of U.S. exports to Japan.

In spite of the total liberalization of capital flows in 1980, it has been said that the institutional arrangements, including those Japanese business customs which are influenced by the Keiretsu[112] ("oligopolistic industrial groups" each of which centers on a major bank and a Sogoshosha), have blocked the growth of FDI in Japan. The Structural Impediments Initiative (SII) talks between the two governments, started in 1989, have aimed at increasing U.S. exports to Japan[113] although this type of comprehensive approach to adjust trade imbalances implies that "virtually everything affects" trade, and will finally result in managed trade.[114] Since 1990, the Japanese government has taken measures to alter structural obstacles to balanced trade, including business customs, lest they should impede the growth of general export to Japan. The implication is that the removal of institutional obstacles to the growth of FDI has been carried out. The Japanese government also has announced that it will encourage the increase of FDI in Japan by adopting more such policies in the future.[115]

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[111] The Economic Planning Agency, 321; Sakurai,; The JETRO, 96; after entering of the Japanese market, foreign firms have faced difficulties in their operations, such as social and cultural differences between their people and those of Japan. These difficulties have discouraged increases in FDI and have made FDI withdraw from Japan.

[112] Chalmers Johnson emphasizes the nationalistic approach of the Japanese government to the Keiretsu. He argues that after World War II, the government supported the emergence of the Keiretsu, most of which have their origins in the Zaibatsu, by assigning non-affiliated firms to specific sogoshosha in order to increase in the total efficiency of the Japanese economy, Johnson, 206.

## The Role Played by the Sogoshosha

Japan's large general trading companies, the Sogoshosha, were fostered by the Meiji government as an instrument of economic nationalism[116] at a time when Japan faced military and economic threats from Western imperial states and needed urgently to catch up to them in the late eighteen century. The Sogoshosha grew rapidly and have played many important roles in the Japanese economy.[117] They contributed largely to the growth of Japanese FDI in the late 1960s and early 1970s when Japanese firms made FDI in labor-intensive manufacturing industries and in resource-related industries in the developing states.

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[113] More than two hundred structural impediments were initially defined by the U.S. government. They included the high savings rates of Japan, Gendai Yogo no Kiso Chishiki (The Basic Knowledge about Contemporary Important Words), 1991, ed., s.v. "the Japan-U.S. Structural Impediments Initiative talks."

[114] Ostry, 77.

[115] The Economic Planning Agency, 321.

[116] The government expected them to "Japanize" the Japanese trade which was largely controlled by foreign business at that time, supply raw materials for industrialization and reduce the manufacturers' burdens in trading their products.

In the case of FDI in labor-intensive manufacturing industries, they organized Japanese investors, introduced them to local partners, and participated in FDI in the form of minority share-holding. The collective style of FDI made risk-sharing possible among Japanese firms.[118] The Sogoshosha provided investors with a general know-how of overseas business activities and dealt favorably with the investors' exports from the host states since many of the Japanese investors were small- and medium-sized firms without enough resources and little experience in international business.[119]

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Alexander K. Young, The Sogo Shosha: Japan's Multinational Trading Companies, (Tokyo: Charles E. Tuttle Company, 1979), 24.

[117] For the different kinds of the Sogoshosha, see Ibid., Chapter 2.

[118] Ozawa, Multinationalism, 186.

[119] Kiyoshi Kojima and Teratoma Ozawa, Japan's General Trading Companies: Merchants of Economic Development, (Paris: the Organization for Economic Cooperation and Development, 1984), 24; Ozawa, Multinationalism, 31-32; Tho, 23-25.

In the case of FDI in resource-related industries, including the D & I and the resource-related mega-projects, the Sogoshosha organized Japanese investors within their own Keiretsu, each of which centers on a major bank and a Sogoshosha.[120] Thus the Sogoshosha made FDI into a complete package.[121] Hence, each of the Japanese firms was smaller and had fewer functions compared with the American and European vertically-integrated multinationals. For example, the Sogoshosha organized most of the resource-related FDI in the Middle East that rapidly increased after the oil crisis in 1973.[122]

However, since late 1970s, the importance of the Sogoshosha has decreased for the following reasons: (1) a decline in new FDI and in mega-projects in resource-related industries followed the post-oil crisis recession and the structural changes made to Japanese industry; (2) Japanese manufacturers started trading without using Sogoshosha in late 1970s as they acquired expertise as MNCs.

Facing this and the decrease in their trading margins caused by the rise of the yen, the Sogoshosha increased their own FDI in manufacturing industries in the forms of full- or majority-ownership. This helped them increase their profits acquired through FDI. They also increased their FDI to reinforce their overseas offices and to engage further in the lucrative intermediary business of trade between states other than Japan.[123] However, the Sogoshosha's new FDI has not significantly influenced total Japanese FDI.

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[120] Ozawa, Multinationalism, 187.

[121] Ibid., 185-191.

[122] Ibid., 145.

## Conclusion

Domestic factors which resulted from state-led economic growth greatly influenced the various aspects of Japanese FDI in the early post-war period. The Japanese economic-nationalist government tightly controlled almost all economic activity and closed the economy off from influences from the international sphere in order to promote economic growth efficiently. A stable international economy under the U.S. hegemon contributed to creating these particular circumstances. Under such conditions, the government was able to use FDI as a tool to realize Japan's planned economic growth.

However, as the hegemony of the U.S. declined, as the economic interdependence of states grew, and the integration of the Japanese economy into the international economy advanced after the 1970s, changes in the international sphere have increasingly influenced Japanese FDI. The gradual deregulation of the Japanese economy has reinforced this trend. Meanwhile, Japanese firms have become MNCs, which make

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[123] Yoshi Tsurumi, Sogoshosha: Engines of Export-Based Growth, rev.ed., (Montreal: The Institution for Research on Public Policy, 1984), 47-51.

FDI as a sophisticated business strategy, and along with this, some of the characteristics of Japanese FDI have become outmoded. FDI has became an important activity in the economy, and the government has lost its formerly strong influence over FDI.

To cope with the resource-scarcity enhanced by state-led economic growth, Japanese investors adopted D & I in cooperation with the government. Since the oil embargo demonstrated resource-dependency, the government devoted itself more to securing stable supplies of raw materials for industry in order to reduce the dependency of Japan on other states and MNCs.

The Sogoshosha played a promotional role in the increase of Japanese FDI. However, as Japanese firms have gained the expertise necessary to make FDI and to deal with international trade, the importance of the Sogoshosha in this capacity has been decreasing.

# CHAPTER FOUR - Development and Foreign Direct Investment of the Japanese Pulp and Paper Industry

## Introduction

This chapter argues that the growing influence of the international political economy since the 1970s has led the Japanese pulp and paper industry to make foreign direct investment(FDI). The increase of international influence on the industry was brought about by structural changes in Japanese industry and new developments in the global political economy: the relative decline of the United States' economic hegemony, the growth of international economic interdependence, and a greater concern for the environment. The industry's dependence on raw materials from overseas and its energy-consuming production-processes make it especially vulnerable to these developments.

In the 1970s and early 1980s, changes in the domestic and international political economy were detrimental to the pulp and paper industry, and certain features of the industry itself worsened the outcome. As a result, the industry's financial health was weakened considerably. A strong government in Japan supported the industry's recovery. After that recovery, incidents in the domestic and international spheres in the late 1980s countered the effects of the previous era: the industry became strong enough to make FDI in pursuit of profit and to avoid the problems which it had previously faced. However, the public's growing concern about global environmental issues has led to fundamental changes in the orientation of FDI.

### The Period of Domestic Development

#### (1) Beginnings of the Dependency on Overseas Suppliers

The Japanese pulp and paper industry has been the world's second largest producer of paper since 1972.[1] Japanese consumption of paper per capita was the eleventh highest in the world during the same year, and by 1987, the ninth highest (see APPENDIX 4).[2] The demand for paper products in Japan was very nearly satisfied by supply from the industry[3]. For example, Japanese importation of paper products was 3.9 percent, and the exportation 3.6 percent, of the total production of the industry in 1987. The business climate of the industry depends on the domestic demand.[4] The basic raw materials for the industry are wood chips, and about 40 percent of the supply of chips has been imported since the

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[1] Hiroshi Asaoka, Kami Palupu(Paper and Pulp), (Tokyo: Nihon Keizai Shinbun Sha, 1989), 47.

[2] Ibid., 11, Table 1-2, 47.

[3] Ibid., 56.

[4] The Federation of Economic Organizations, the Industrial Structure Division of the Industrial Issue Committee, Wagakuni Sangyo no Endaka e no Taio to Kongo no Shinro: Dai II Bu Kakuron (The Measures of the Japanese Industries to the Yen Appreciations and the Prospective Course: Part II The Details), (Tokyo: The Federation of Economic Organization, 1989), 57.

1970s.[5] The main suppliers of wood chips are the United States, Canada and Australia. The United States has been the largest supplier of softwood chips and it supplied 58 percent of imports in 1990; Canada, the second largest, supplied 24 percent. As for hardwood chips, Australia has been the largest supplier, accounting for 37 percent of the import; the United States, the second largest, supplied 29 percent. Because of limited domestic supply, securing raw materials from overseas has been the industry's greatest concern since the early 1960s.[6]

Domestic producers were able to meet the industry's demand for wood chips until the late 1950s, because the Japanese had stopped using wood as fuel for their homes after World War II,[7] and the consumption of raw lumber in Japan was not heavy. However, the industry gradually faced a domestic shortage, although Japan held a certain amount of forest resources. This was brought about by a decline in the lumber industry and a shortage of young workers in that industry, with both factors being the result of state-led industrialization. The few young workers in the marketplace were absorbed by other manufacturing industries such as the automobile manufacturing. Furthermore, the demand for timber expanded during the 1950s, spurred on by state-led high economic growth, resulting in a restricted domestic supply and in price hikes.

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[5] Yano Keizai Kenkyujo (Yano Economic Research Institute Ltd.), Kami Palupu Sangyo: Ju Nengo (Pulp and Paper Industry: Ten Years Later, (Tokyo: Yano Keizai Kenkyujo, 1987), 177: Asaoka, 53, 55.

[6] In the report of 1983, private ownership of forests by Japan's largest producer, Oji Paper, was one twenty-eighth in terms of area, and one fortieth in amount of lumber, that of the world's largest producer, International Paper. Yano Keizai Kenkyujo, 196, Table 6-3-6.

[7] Asaoka, 44.

The government curtailed the pulp and paper industry's new investment for plants and equipments in 1958 in order to slow the increase of consumption of timber.[8] It subsequently removed import restrictions on timber in 1961 and 1964.

The Japanese pulp and paper industry felt the necessity of securing an independent supply of wood chips, and started importing from the United States using their own "chip carriers" in 1963.[9] This use of imported wood chips contributed to the development of the industry[10], as well as to a dependence on overseas suppliers. Furthermore, the pulp and paper industry acted as a bloc to make FDI to secure the supply of wood chips. It started experimental afforestation in the South Seas. Individual producers also made FDI -- five FDIs were made to produce pulp. However, these measures were still "tentative"[11] because, since 1963, the import of wood chips from overseas suppliers had been increasing. It hit a record level in 1979: 46.1 percent of the total supply, and a correspondingly greater dependency on overseas supplies.[12]

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[8] Ibid., 40.

[9] Ibid., 44-45.

[10] Yano Keizai Kenkyujo, 160.

[11] Kenji Ohkawa, ed., Kami Palupu Gyokai (Pulp and Paper Industry), (Tokyo: Kyouiku Sha, 1975), 231.

Meanwhile the industry grew steadily (see APPENDIX 5) because of domestic demand spurred on by economic development, the subsequent westernization of people's way of life, and the industry's technological innovations.[13]

### (2) Recycling

As a result of increases in Japan's consumption of paper and a shortage of raw materials, the industry put much emphasis on recycling waste-paper. The recycling system developed gradually as general public recognition of resource-scarcity helped promote recycling. Although there was a slight downturn in the 1960s and early 1970s, the ratios of recycled waste-paper to total production input of pulp and paper were 15, 38, and 49.6 percent in 1951, 1963 and 1988 respectively.[14]

### (3) Pollution

People in many regions of Japan had suffered from industrial pollution since the late 1960s as a result of rapid economic growth and the national and local governments' apathy towards their suffering and environmental damage. The governments did little to introduce laws and regulations to control pollution. The degree of certain kinds of pollution was so severe that people in some regions contracted fatal diseases such as mercury poisoning, and many fishermen had to give up their businesses because of coastal pollution.

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[12] "Waga Kuni Kamipa Sangyo to Kokusai Kyosoryoku: Seihin Yunyu Kakudai wo Chushin to Shite" (The Japanese Paper and Pulp Industry and Its International Competitiveness: the Increases of Paper Product-Import to Japan), Kaigin Chosa (The Japan Development Bank Research), 58 (February 1983): 98.

[13] Yano Keizai Kenkyujo, 160-164.

[14] Asaoka, 46; Shigyo Times (Pulp and Paper Times), 946, (1 December 1989): 33.

In many cases, the polluters were heavy and chemical industries. They, and the governments, refused to acknowledge the direct link between their industrial waste and ecological damage and incidence of disease; until, that is, being defeated in lawsuits over pollution issues. After losing cases and receiving accusations from the general public, the Japanese government finally and reluctantly introduced stricter legislation in 1973. Some local governments adopted regulations which were more stringent than national standards.[15]

The Japanese paper and pulp industry had been one of the polluting industries up to the mid-1970s and was deeply involved in the litigation mentioned above. Although pulp and paper effluent and pollutants did not cause serious diseases in humans, the industry's waste polluted coastal areas and caused considerable damage to local fisheries. When fishermen and their citizen-supporters brought suit, individual companies were required to pay significant indemnities.[16] In addition, pulp and paper companies were required to install anti-pollution devices in observance of newly enacted environmental laws and regulations. The investment in anti-pollution devices was a heavy burden for the industry; for example, it was 24.8 percent of the total investment for plants and equipments in 1969[17] and 24.1 percent in 1975[18]. Incidentally, the Japanese government was generous to the industry, allowing it for five years to observe less strict temporary standards controlling water pollution.[19]

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[15] Ohkawa, 89, 92.

Installing anti-pollution devices in existing facilities was often more expensive than the cost of constructing new facilities incorporating those devices. So, facing stricter environmental laws as well as increasing opposition to the construction of their new production facilities from residents in many areas, polluting industries found FDI more attractive for the expansion of their production capacities. It should be noted that FDI in developing states is attractive to polluters since environmental regulations in these states are often much less demanding than those in developed states. At the extreme, some states show an intention to invite polluting industries without any consideration of the damage to people and the environment.[20] This is because the "foremost objective" of the governments of most developing nations remains industrialization.[21]

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[16] One of the so-called "Big Four Pollution Cases" in Japan was "The Tagonoura Bay Effusion Case", fought between residents and fishermen, and four paper and pulp producers (Daishowa, Koakogyo, Daiko and Honshu) and the Shizuoka Prefecture. The defendants were indicted in 1970. For details, see Toshihiko Koda, Tagonoura no Hedoro wa Kiezu (The Dirty Effusion in The Tagonoura Bay Never Disappears), (Tokyo: Asahi Shinbun Sha, 1979).

[17] Nikkei Sangyo (Tokyo) Shinbun (Nikkei Industry Newspaper), 14 February 1977.

[18] Nikkei Sangyo (Tokyo) Shinbun (Nikkei Industry Newspaper), 11 December 1976.

[19] Mr. Shimizu, an official of the Environmental Agency, interviewed by author, Tokyo, Japan, 6 January 1992.

However, in this period, the Japanese pulp and paper industry was suffering from the recession which followed the oil crisis. The cost of implementing environmental legislation served only to exacerbate their fiscal problems. As a whole, the industry lost its ability to make widespread FDI. There were only two noteworthy cases of FDI made by producers in the aftermath of the pollution issue: one by Daishowa, the other by Jujo and Sanyo-Kokusaku Pulp. The purpose of both was pulp-making, the main source of pollution in the industry.[22]

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[20] Former Philippine president Ferdinand Marcos said: "Philippine is ready to accept the Japanese factories which will be shut down in Japan because of their pollution," Yomiuri(Tokyo) Shinbun(Yomiuri Newspaper), 29 January 1977, quoted in Nihon Bengoshi Rengokai(the Japan Bar Association), Nihon no Kogai Yushutsu to Kankyo Hakai: Tonan Ajia ni Okeru Kigyo Shinshutsu to ODA(Export of Pollution and Environmental Destruction: Business Expansion of Japanese Corporations in the Southeast Asia and the ODA), (Tokyo: Nihon Hyoron Sha, 1991), 80.

[21] Gautam Sen, The Military Origin of Industrialization and International Trade Rivalry, (New York: St. Martin's Press, 1984), quoted in Robert Gilpin, The Political Economy of International Relations, (New Jersey: Princeton University Press, 1987), 33.

## International Influence

Changes in foreign economies and in international political economy had began to influence Japan in the 1970s. The decline of the United States' international economic hegemony and the emergence of international economic interdependence were the chief causes of these changes. As the Japanese economy became increasingly integrated into the international economy, the Japanese pulp and paper industry, like the rest of Japan's industries, became increasingly sensitive to changes in the international and foreign economies. The Japanese government became more involved in supporting the industry. It should be noted that the industry had depended more heavily on the government[23] than the other industries which have been "responsive dependen(t)."[24] Meanwhile, its dependency on overseas suppliers of wood chips had been increasing.

### (1) The First Oil Crisis

The industry is a large consumer of energy. Even after the two oil crises, and after its own extensive conservation efforts, it represented 7.9 percent of Japan's total industrial consumption of heavy oil, coal and electricity, while accounting for only 1.4 percent of the total value of Japanese industrial output in the fiscal year 1986.[25] Higher energy costs caused by the first oil crisis was a weakening blow to the industry. In response, the MITI allowed the industry to form "recession cartels" in 1977. Under the protection of the recession cartels, the industry made efforts to reduce its energy consumption. This severe business climate discouraged new FDI by individual producers.

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[22] Toyo Keizai Shinpo Sha ed., Kaisha Betsu Kaigai Shinshutsu Kigyo 1991/92 Nen (Companies' Overseas Business 1991/1992), (Tokyo: Toyo Keizai Shinpo Sha, 1992), 146, 147, 149.

[23] Yano Keizai Kenkyujo, 156.

[24] Gary D. Allinson, 43-45, quoted in Chalmers Johnson, MITI and the Japanese Miracle: The Growth of Industrial Policy, 1925-1975, (Tokyo: Charles E. Tuttle Co., 1982), 24.

### (2) Appreciation of the Yen

One serious issue for the industry has been the appreciation of the value of the yen.[26] The rapid increases from December 1975 onward made the industry face harder competition with foreign paper-producers. In the early stages of the increase, the industry enjoyed lowered prices of imported wood chips. But the further rise of the yen -- i.e., further declines in the prices of imported paper -- forced the industry to cut prices on their own products in order to maintain their market share in 1978.[27]

### (3) Government Support for Cooperative FDI

Economic nationalist governments intervene significantly in the market to promote the development of industry. The Japanese government began to support D & I of the Japanese pulp and paper industry in the late 1970s in response to requests from the industry suffering from the bad business climate. The government supported industry's cooperative D & I in Brazil and the South Pacific. It provided funds for D & I in Brazil through the ODA.[28] The fundamental reasons for government involvement were that it desired to diversify the dependence of the industry on foreign suppliers of raw materials and to transform Japanese industries to make them cleaner and less resource-consuming. Pollution-causing and resource-consuming industries and production processes, such as pulp making, were encouraged to move abroad.[29]

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[25] The Federation of Economic Organization, 57.

[26] Yano Keizai Kenkyujo, 192.

[27] Nihon Keizai Shinbun (Japan Economic Newspaper), 4 April 1978.

### (4) Chip Shock

What caused the industry more critical damage than the oil crises was the so-called "chip shock" in 1980. Triggered by large price-increases in American softwood chips against the industry, the shock resulted in sudden price-hikes in the whole wood-chip supply -- including the domestic supply. The fundamental cause of the "chip shock" lay in the industry's very dependency on American suppliers. These suppliers mostly produced softwood chips: the ratio of imported softwood was about 58.2 percent to the total consumption of softwood chips in 1979.[30] Of the imported softwood chips, about 81 percent were supplied by American producers in 1981.[31] The suppliers formed a producer cartel, albeit a tentative one, and increased softwood-chip prices by 67.3 percent in January 1980.[32] They selected Weyerhaeuser, an American multinational wood-chip supplier, to negotiate with the Japanese pulp and paper industry. Since the company had hitherto exerted a great influence on the world chip-prices because of its many deals in the world wood-chip market[33] and the industry was heavily dependent on the American producers, the industry could not help but accept price increases.

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[28] The one in Brazil was started by a firm and became the Japan-Brazil Paper and Pulp Resource Development in 1970. Seventeen industry firms and one general trading company participated in the project. The South Pacific project of the Japanese Overseas Afforestation Association, begun in the 1970s by eleven firms, has made experimental afforestation in four states. The MITI has been leading and supporting the project. Shigyo Times (Paper Industry Times), 946 (1 December 1989): 33.

[29] Okawa, 228.

The "chip shock" was a turning point for the industry,[34] signalling its need to diversify foreign sources as well as to reduce its dependency on imported wood chips. It succeeded in reducing dependency: the ratio of imported softwood chips to total consumption was decreased from 58.2 percent in 1979 to 49.7 percent in 1981.[35] The industry increased its consumption of domestic wood chips and asked the government to promote a domestic supply.

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[30] Kaigin Chose (the Japan Industrial Development Bank Research): 98.

[31] Nihon Seishi Rengokai(Japan Paper Association), Pulp Wood Division, Pulp Zai Tokei(Pulp Wood Statistics), (Tokyo: Nihon Seishi Rengokai(Japan Paper Association): 1979), 13.

[32] Daishowa Paper Mfg. Co., Ltd., Daishowa Seishi Gojyunen Shi (Daishowa Paper Fifty-Year History), (Shizuoka: Daishowa Paper Mfg., Co., Ltd., 1990), 399.

[33] Ibid., 401.

[34] Ibid., 401

### (5) The Second Oil Crisis

The oil price-hikes of the second oil crisis in 1979 caused further deterioration of the international economy and was an additional blow to the Japanese pulp and paper industry. The average return on sales in the industry was only 1.5 percent, less than half the average for Japanese manufacturing industries. Responding to this critical situation, the government bailed the industry out. In addition to the "recession cartels," the MITI carried out administrative guidance to improve the pulp and paper business and applied a special law to the industry. The law allows weakening industries to create cartels and collectively control new investment for plants and equipments.[36] The industry formed cartels over more of their products and controlled the investment of each producer.

## The Proposal from the MITI

Economic nationalist governments desire to reduce dependencies of their economies on specific national economies or MNCs. The Japanese government proposed a reduction in the pulp and paper industry's dependence on overseas suppliers. In March of 1981, the Pulp and Paper Committee of the MITI's Industrial Structural Council announced its long-term proposal for improvement, entitled "The Pulp and Paper Industry in the 1980s." The proposal expressed the government's decision to devote itself to supporting the industry's efforts to secure a stable supply of raw materials in response to the "chip shock." It strongly recommended that the industry decrease its dependency on a certain region, the United States, by diversifying the sources of supply by various means. The government preferred D & I, and indicated a strong financial commitment to the initiative.

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[35] Kaigin Chosa (The Japan Development Bank): 98.

[36] Asaoka, 81; The Federation of Economic Organization, 58.

The main points of the proposal were the following: 1) promotion of D & I of wood-chips, pulp or paper, based on afforestation; 2) promotion of domestic afforestation to secure domestic supply of wood-chips; 3) promotion of recycling of waste-paper; 4) technological development to realize the utility of hitherto unused species of trees, and more efficient exploitation of existing raw materials; 5) expansion of overseas afforestation; 6) increases in the government support to those instances of D & I which include afforestation;[37] 7) greater involvement of banks and sogoshosha -- strong agents in the Japanese economy which had cooperated with the government in the state-led economic growth -- in D & I as supporters of the industry.[38]

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[37] Another factors which made the government support the investments was the fact that investors had to wait a considerable time before gaining the return from their investments, and had to owe the "country risks" of the resource-producing states.

## The Era of FDI

### (1) Recovery of Business

The industry recovered from its critical condition with the help of the MITI's interventions and its own initiatives (including reduced energy-consumption), and it recorded its highest-ever profit in 1984.[39] After this, conditions favourable to the industry persisted in the Japanese economy. There was a reduction in production costs because of the rapid appreciation of the yen.[40] Then there was a "domestic demand-led" boom brought about by policy coordination between Japan and the United States to solve the trade imbalance. Furthermore, the liberalization of the Japanese financial system--partly in response to pressure from the Untied States--had promoted a domestic stock-market boom, and this boom increased in the demand for paper. As a result, industry profit continued to rise.[41] Finally, application to the industry of the special law for weakening industries was ended in February, 1988.[42] The amount of their domestic investment for plants and equipment reached record high levels from April, 1987 to March, 1988.[43]

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[38] The Ministry of International Trade and Industry, the Industrial Structural Council, the Paper and Pulp Committee, Hachiju Nenday no Kamipa Sangyo Bijon (The Paper and Pulp Industry in the 1980s), (Tokyo: The Ministry of International Trade and Industry, 1981), 15-16, 9-10.

[39] Yano Keizai Kenkyujo, 177.

[40] Nihon Keizai Shinbun(Japan Economic Newspaper), 31 October 1987; the appreciation of the yen made imported wood-chips 30 percent cheaper than domestic ones in 1988, Nihon Keizai Shinbun(Japan Economic Newspaper), 15 July 1988.

### (2) Prospective Domestic Supply of Wood Chips

The MITI had proposed the lessening of dependency on overseas suppliers. In 1983 The Ministry of Agriculture and Forestry optimistically planned the future expansion of domestic afforestation. This implied an increase in the future domestic supply of raw materials to the industry. However, in 1985 the industry found by its own research that the future domestic supply of wood-chips would decrease.[44] The reasons for this projected decline were: first, the expected decline of domestic afforestation, which by 1982 had already shrunk to 38.7 percent of a record high in 1961; second, the low enthusiasm of local governments (who have jurisdictions over most of the forests in Japan) for cultivating hardwood trees which were still available at competitive rates on the world market.[45] The findings were shocking news to the industry, and it realized that the time for relying on the domestic supply would soon end, and that the most reliable way to secure raw materials would be FDI -- the best way, probably, D & I.[46]

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[41] The Japanese pulp and paper producers had made unusually high profits from 1984 to 1988. Nihon Keizai Shinbun(Japan Economic Newspaper), 29 April, 1988.

[42] Nihon Keizai Shinbun(Japan Economic Newspaper), 20 January 1988.

[43] Nihon Keizai Shinbun(Japan Economic Newspaper), 4 February 1988.

[44] Nihon Seishi Rengokai (Japan Paper Association), Kokusan Palupuzai Kyoukyu Mitoshi(the Prospective Supply of Domestic Wood-Chips, (Tokyo: Nihon Seishi Rengokai(Japan Paper Association, 1985), passim.

### (3) Globalization

Cheaper foreign assets afforded by a stronger yen after the Plaza Accord of 1985 encouraged producers of the industry to expand overseas. In addition, the industry had achieved record-high profits that year. The rapidly growing world-wide demand for paper products to supply new office machineries seemed to be a promise of further increases in sales, a "go-sign" for making additional FDI in the industry. The products of foreign competitors, significantly those of U.S. producers, were being absorbed by the great demands in their own markets, so Japanese producers did not need to worry about a massive influx of cheaper foreign paper products in spite of the rapid appreciation of the yen.[47] The price-hikes of wood-chips caused by a growing demand for them in the late 1980s stimulated the industry to make FDI in order to secure cheaper chips.[48] Lower energy-costs abroad encouraged FDI; for example, the costs of oil and electricity in the United States, compared to those in Japan, were 70 percent and 65 percent respectively.[49] It should be noted that defensive considerations, such as the anticipated decline in domestic supply of raw materials, also encouraged FDI. Thus, corporations started to make FDI in earnest. This "late globalization"[50] of the industry finally got under way in the second half of the 1980s(see APPENDIX 6).

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[45] Ibid., 3-5.

[46] Ibid., passim.

[47] Nihon Keizai Shinbun(Japan Economic Newspaer), 4 February 1988.

The business activities of the industry's FDI have covered various ranges of those activities generally attributed to MNCs. Some of the companies who made FDI have grown to be full-fledged MNCs. Among the theories of FDI, the "industrial organization theory of vertical integration"[51] effectively explains the industry's FDI. The theory maintains that MNCs "place the various stages of production in different locations throughout the globe," and "a primary motivation of foreign direct investment is to take advantage of lower costs of production, local tax benefits,... The result of this internationalization of the production process has been the rapid expansion of intra-firm trade," of "the import and export of components and intermediate goods."[52] MNCs that have "technical expertise, managerial skills, or economy of scales" can compensate the cost of their overseas business and can "compete successfully" with firms in the host states.

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[48] Nihon Keizai Shinbun(Nihon Economic Newspaer), 15 December 1989.

[49] Yano Keizai Kenkyujo, 195.

[50] Nihon Keizai Shinbun(Japan Econmic Newspaper), 4 February 1988.

[51] Paul R. Krugman, "Economics of Scale, Imperfect Competition, and Trade: An Exposition," 1981, unpublished, quoted in Gilpin, 234.

The Japanese pulp and paper producers who made FDI have been carrying out intra-firm trade; making wood-chips or pulp overseas and exporting them to Japan for their paper-production, thereby making use of the technological advantages and large production-scales which are at their disposal as the world's second largest paper producers. They can sell finished products in the host countries as well as to other countries.[53]

## New Challenge to the Industry

### (1) Increasing Importance of Conservation of Forests

"The growing salience of policy issues arising in connection with global environmental changes - like ozone layer depletion, global warming and the loss of biodiversity - has already stimulated a surge of interest in responses featuring agreements that call for sustained international cooperation."[54]2 The United Nations Environmental Program

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[52] Gilpin, 237-238.

[53] Even some producers have reverse-exported them to Japan.

[54] Oran Young, "Global Environmental Change and International Governance," Millennium: Journal of International Studies, Vol. 19, No. 3, (Winter 1990): 337.

(UNEP), "which is specifically assigned a 'catalytic and coordinating role' within the UN system,"[55] was established in 1972 and has encouraged actions directed at solving international environmental problems. Confronted with public pressure regarding these problems, inter-governmental organizations have created forums to seek measures to deal with them.[56] Non-government organizations, including scientific and research institutes and think tanks, have also been involved in urging governments and international organizations to formulate policies for coping with the problems.[57] Additionally, the philosophy of sustainable development, which emphasizes the maintenance of ecosystems' capacities for self-renewal and restricts practices which endanger them,[58] has been widely accepted, at least in the developed states[59], as an appropriate approach to global environmental issues in 1980s.

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[55] Glen Plant, "Institutional and Legal Responses to Global Climate Change," Millennium: Journal of International Studies, Vol. 19, No. 3 (Winter 1990): 414.

[56] Young, 416, 417.

[57] Marvin S. Soroos, "The Tragedy of the Commons in Global Perspective," in Charles W. Kegley, Jr. and Eugene R. Wittkopf, The Global Agenda: Issues & Perspectives, 2d ed., (New York: Randam House, 1988): 345, 347; Peter M. Haas, "Obtaining International Environmental Protection Through Epistemic Consensus," Millennium: Journal of International Studies, Vol. 19, No. 3. (Winter 1990).

[58] David Pearce, "Economics and the Global Environmental Challenge," Millennium: Journal of International Studies, Vol. 19, No.3, 365-367; Nihon Bengoshi Rengokai(the Japan Bar Association), 167-168.

The photosynthetic activity of rain forests is crucial to their regional ecosystems as well as to the global ecology. However, rain forests are being logged at a rate of 1.7 billion hectares per year.[60] To promote more appropriate usage and preservation of global rain forests, the United Nations Food and Agriculture Organization (FAO), which has worked with UNEP on environmental issues, created the Tropical Forest Action Program in 1985. Finally, the International Tropical Timber Organization (ITTO), to which Japan is the host-state, was established by the United Nations in 1986.

Japan has been criticized internationally for logging large areas of rain forests and for importing the world's largest amount of lumber from rain forests.[61] The ITTO showed great concern over logging by Japanese overseas firms. Ninety percent of Japan's import of rain forest lumber comes from Malaysia, especially Sarawak Province, where Japanese subsidiary companies have been logging carelessly. The Sarawak Report of the ITTO in 1990 warned that the entire rain forest of Sarawak would disappear in eleven years if the cutting continued at the then-current rate, and suggested a 30 percent decrease in logging was appropriate for sustainable development.[62]

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[59] Some developing nations have been opposed to the idea because sustainable development would slow or stop their national development.

[60] The depletion was 1.1 billion hectares annually a decade ago, Nihon Keizai Shinbun(Japan Economic Newspaper), 5 November 1991.

[61] Hiroyuki Ishi, Chikyu Kankyo Hokoku (Global Environmental Report), (Tokyo: Iwanami Shonten, 1988), 96; the sogoshosha were boycotted by citizens in Europe and Australia in 1988 because sogoshosha are the major importers of lumber from rain forests, Nihon Bengoshi Rengokai(The Japan Bar Association), 37.

In response to the general criticism, the Forest Agency of Japan tabled its 1990 interim report on the rain forest issue, which urged that Japan should import "produced" trees, i.e., planted trees, in order to carry out sustainable development. But early realization of this proposal is unlikely.[63] The Japanese government also provided US $20 million to the ITTO as fund-money for the reserve rain forests.[64]

### (2) The Response from the Industry

The "industry's dependency" on softwood from the rain forest has not been heavy; the portion of rain forest products in the industry's total import of forest products has been in the range of two to five percent.[65] In spite of this fact, it should be noted that some Japanese producers' subsidiaries, established by their FDI, have caused environmental/ecological destruction by logging rain forests.[66] After intense pressure from environmental groups concerned with the depletion of rain forest, the industry recognized the public's concerns.[67] Responding to these developments, the industry and the MITI have begun to study measures for dealing not only with the concerns about the rain forest, but also with the growing environmental concerns at the global level. In addition, the association of the industry proposed the following steps: the promotion of afforestation in the tropics and of technical assistance to the states in the areas in their afforestation; further efforts to boost recycling of waste-paper; adoption of new technologies to reduce the emission of carbon dioxide.[68]

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[62] Nihon Bengoshi Rengokai(the Japan Bar Association), 21, 28.

[63] This is because the sogoshosha, which have been cutting and importing rain forest lumber, did not accept the ITTO's suggestion of a 30 percent decrease. Instead, they set their goals at a level of 10 to 15 percent, ibid,, 36.

[64] Ibid., 194.

[65] "Chikyu Kankyo Mondai to Kami Pulp Sangyo (Global Environmental Issues and the Pulp and Paper Industry)," Shigyo Times (Paper and Pulp Industry Times), 946 (1 December 1989):32.

Both industry and government allocated more funds to the project in Brazil in 1988.[69] In the same year, fifteen producers decided to construct a wood-chip factory based on

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[66] For example, in Papua New Guinea the 92.8 percent Honshu Paper-owned logging company has been accused of indiscriminate logging by the residents and the environmental groups supporting them, Kaoru Kato, "Shrarezaru Nyu Ginia: Shinrin Bassai(Unknown New Guinea: Forest Cutting", Sekai (World), (November 1991): 231.

[67] Shigyo Times (Paper and Pulp Industry Times), 946, (1 December 1989):27.

[68] Ibid., 35.

[69] Ibid., 33.

Eucalyptus-afforestation by farmers' cooperatives in Thailand,[70] a nation which has also been suffered from "dependency" because of its export of just a few agricultural products.

Individual producers rushed to begin afforestation in Japan and abroad: from 1989 to 1991, three large producers started new afforestation and one producer doubled its rate of afforestation.[71] It is important to notice that these FDIs were made not only to the end of securing raw materials but also in response to increasing public concerns and pressure from environmental groups.

## Conclusion

Since the 1970s, changes in international and national economies have influenced the Japanese pulp and paper industry, which has been dependent on raw materials from overseas suppliers. These changes are now the most important determinants of FDI in the industry. The industry's business climate had deteriorated considerably, mainly because of incidents in the international sphere, from the first oil crisis until the early 1980s. For this reason, the Japanese government supported the pulp and paper industry significantly, and the industry relied on that support. In order to avoid certain difficulties during this period, making FDI would have been a good option for the industry, but it was too weak to do so.

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[70] Ibid., 33.

[71] Daio, Mistubishi started afforestation in Chile, Oji in Japan, and Honshu doubled its efforts in Papua New Guinea, Nihon Keizai Shinbun(Japan Economic Newspaper), 29 June 1990, 1 November 1990, 22 July 1991.

The industry recovered by the mid-1980s. The continuing favourable economic circumstances in the late 1980s brought about policy coordinations mainly between Japan and the United States, and resulted in profits high enough for FDI to be feasible. The appreciation of the yen made foreign assets cheaper. Finally in the late 1980s, the industry began to make FDI full scale. The purposes of this FDI included securing future supplies of raw materials.

Growing popular awareness of global environmental problems has caused increased pressure on the industry and become a new impetus to make FDI. Some of the producers have already made FDI based on afforestation to answer these concerns at the global level. The growth of popular environmental concern has led to another turning point for the industry, and a test of the corporate philosophy of each producer.

# CHAPTER FIVE - Issues in the Foreign Direct Investment by the Japanese Pulp and Paper Industry: A Pulp Mill of Daishowa in Alberta

## Introduction

This chapter studies the difficulties encountered by one Japanese multinational pulp and paper producer, Daishowa Paper Manufacturing Co., Ltd., in its foreign direct investment (FDI) in Alberta in the late 1980s. The host government needed to invite foreign investors to stimulate the province's economy, and so made certain concessions to Daishowa. The company subsequently made FDI for production of bleached kraft pulp in order to secure raw materials and maximize profit in its global production system. But Daishowa faced strong opposition from environmental groups and the public, as well as from the Lubicon Indians, a band of Canadian native Indians.

Daishowa abided by Alberta's environmental regulations and by a plan of forest management defined by an agreement between the company and the government, but they were unable to respond adequately to growing environmental concerns. The rising concern was a reflection of increasing awareness of environmental issues at the global level. Environmental and other pressure groups were concerned about the pollution from the discharge of Daishowa's pulp mill, and damage to the forest that would result from Daishowa's methods of logging.

Another challenge came from the Lubicon Indians, whose claimed land overlapped part of Daishowa's cutting area. Facing strong opposition (including an international boycott), after hoping to avoid entanglement in the Lubicon's political negotiations with Alberta and the federal government, the company abandoned its cutting plans. Its activities in the logging of Wood Buffalo National Park were also highly controversial and were successfully challenged in a legal action by environmental groups.

Pressure from domestic interest groups weakened bargaining power of Daishowa vis a vis the Alberta government. Meanwhile, decreased uncertainty of the FDI after the actual investment shifted the power balance[1] further to Alberta's side. The government, having made several concessions to Daishowa, refused to make new ones. Alberta adopted policies affecting Daishowa's interests, which reflected the competition of domestic groups[2] and were not profitable to Daishowa.

The Japanese government itself took no public measures to ease Daishowa's difficulties. This was perhaps because the cost of such measures was prohibitive in various ways, perhaps violating the principle of non-intervention in the international community. It could also be said that the Japanese government's aversion to influencing Canadian domestic political affairs further restrained it from taking action.

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[1] Theodore H. Moran, Multinational Corporations and the Politics of Dependence, (New Jersey: Princeton University Press, 1974), 159.

[2] Ibid., 159-160.

## Political Economy of Alberta

Increasing interdependence among national economies has made each one vulnerable to changes and fluctuations in others. The rapid decline in oil prices in 1986 caused serious damage to Alberta's economy, which depended heavily on the oil industry. Alberta's second major industry, agriculture, was also damaged by the price reductions caused by export competition between Europe and the United States in the early 1980s. The province, which was known for its "economic provincialism," seriously needed to develop new industry and to stimulate and diversify its economy.

Alberta had a vast untouched forest area: the fourth largest of any Canadian province in 1987.[3] Ownership of land and forest resources was under provincial jurisdiction under Canada's federal system. The new Premier of the Alberta government, Don Getty, decided to promote the forest industry as another leading industry, and it established the Forest Industry Development Division within the Department of the Forestry in June 1986. The government intended to promote the industry through assistance to private investors.[4] It decided to emphasize pulp and paper industry as the main sector of its forest-industry promotion[5] because the industry was expected to provide an opportunity to the Albertans to increase value-added investment and employment in the province.

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[3] The Edmonton Journal, 3 May 1987, C8.

Research and development (R & D) upgrades raw materials, transforming them into more efficient industrial input, increasing the viability of an industry by cost-reduction and so forth. The aspen, a hardwood which grows in large area in the province and had been called a weed,[6] became a raw material of pulp making thanks to R & D and increased in its importance to the province.

### Daishowa's Foreign Direct Investment in Alberta

The governments of developed states see MNCs "as a means of increasing national material welfare"[7] because MNCs possess technology, capital, and marketing ability and because their large scale of operation can stimulate the economies of host states. The Alberta government induced Japanese and other multinational pulp and paper manufacturers to make FDI in Alberta. Japan's pulp and paper producers seemed to Alberta to be the likeliest potential sources of FDI: they were concerned about securing raw materials, they depended on overseas suppliers, and they possessed technology capable of processing aspen, as well as capital to make FDI. In addition, Alberta had enjoyed close trade relations with Japan since the 1970s.

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[4] Al Brennan, Executive Officer, the Alberta Department of Forestry, Lands and wildlife, Forest Industry Development Division, paper presented at an investment forum, "From Woodchips to Blue Chips," of Canadian Council of Forest Ministers, Stimulating Investment: A Government Perspective, 2 March, 1989, 14.

[5] Ibid., 3.

[6] Andrew Nikiforuk and Ed Struzik, "The Great Forest Sell-Off," Report of Business Magazine, November 1989, 58.

[7] Robert T. Kudrle, "The Several Faces of the Multinational Corporation: Political Reaction and Policy Response," in Kendall W. Stiles and Tsuneo Akaha, International Political Economy: A Reader, (New York: Harper Collins Publishers, 1991), 236.

### (1) Daishowa

Daishowa Paper Manufacturing Co., Ltd., the parent company of Daishowa Canada, was the second-largest paper manufacturer in Japan.[8] It made its first overseas investment in 1967 and had been active in making FDI.[9] Japan's paper manufacturers only started making full-scale FDI in the mid-1980s. Among them, Daishowa was an active foreign investor, making five new FDIs in North America and two in Australia from 1988 to 1990. The money it invested in new FDI in the late 1980s reached about US $3.1 billion.[10] The company already owned a wood chip factory and pulp mills overseas, parts of its vertically-integrated production system. The president of Daishowa explained that the purposes of the overseas expansion were reduction of production costs, transfer of less value-added production processes overseas, and subsequent strengthening of domestic production, which was highly value-added and required high technology.[11]

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[8] James P. Morrison, General Manager, Edmonton Office Daishowa Canada Co., Ltd., transcript of speech, "Daishowa's Alberta Operations: Meeting Economic Challenges and Public Expectations," Edmonton, 12 March 1992, 2.

[9] It had already made FDI in Australia, British Columbia and Washington State.

Daishowa's overseas business expansion was spurred on by generally good business conditions in the Japanese pulp and paper industry in the late 1980s. There was a strong demand for paper products domestically and worldwide. As a result, Daishowa made record profits in the fiscal year 1986.[12] The rapid appreciation of the yen, the anticipated shortage of the domestic supply of wood chips[13] and the bitter experiences of the "chip shock" in 1980,[14] encouraged

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[10] Nihon Keizai Shinbun (Japan Economic Newspaper), 20 August 1987, 3 December 1987, 18 February 1988, 14 June 1988, 12 April 1989, 24 July 1989 ; Daishowa Paper Manufacturing Co., Ltd., 504.

[11] Takashi Saito, president of Daishowa, interview in Nihon Keizai Shinbun (Japan Economic Newspaper), 21 August 1988.

[12] Nihon Keizai Shinbun (Japan Economic Newspaper), 11 March 1987.

[13] Nihon Seishi Rengokai (Japan Paper Association), Kokusan Palupuzai Kyoukyu Mitoshi (The Prospective Supply of Domestic Pulp Wood), (Tokyo: Nihon Seishi Rengokai, 1985), passim.

[14] After the American wood-chip suppliers announced a large price increase in 1979, Ryouei Saito, then president of Daishowa, declared the company's decision to reduce its dependency on overseas suppliers. He said that the production

Daishowa to make FDI.

### (2) The Conditions of the FDI

"The conditions under which a foreign company will agree to invest must initially reflect both its monopoly control of skills and its heavy discount for risk and uncertainty." Certain concessions must be made to the investor.[15] In addition, "the so-called bursts or waves of emotion and economic nationalism are no less 'rational' ways of testing the strength of" the bargaining position of the host state against MNCs.[16] The Alberta government found Daishowa Paper Manufacturing Co., Ltd. a prospective investor, as Daishowa hoped to establish bleached kraft pulp mills.

The Progressive Conservative government of Alberta made several concessions to Daishowa in order to attract investment. The concessions included subsidies of 65 million Canadian dollars from the Alberta government and 9.5 million Canadian dollars from the federal government for infrastructure development for the pulp mill.[17] They also included the cheapest stumpage fee of hardwood in Canada. The fee was 28 Canadian cents per cubic meter; the same fee on the

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of less value-added products such as pulp, newsprint, and kraft paper was more profitable in North America than in Japan. Daishowa Paper Manufacturing Co., Ltd., Daishowa Seishi Gojyunen Shi (Daishowa Paper Fifty-Year History, (Shizuoka: Daishowa Paper Mfg., Co., Ltd.), 401.

[15] Moran, 159.

[16] Ibid., 169.

[17] The Edmonton Journal, 9 February 1988, F1.

coast in British Columbia was 10.59 and in the interior 8.59 Canadian dollars.[18]

Having won concessions to its satisfaction, Daishowa announced in 1988 that it would construct a bleached kraft pulp mill in the Peace River area, at a cost of 500 million Canadian dollars. The company received twenty-year timber tenure of 40,710 square kilometers of forest area for the mill operation which would primarily process aspen poplar. About 60 to 70 percent of the pulp produced at the Peace River mill would be exported to Japan as processed input for Daishowa's paper mill; the remainder would be divided between export to Europe, Asia and the United States, and sales in Canada.[19] The agreement between Daishowa and the government stated that Daishowa would begin construction of another pulp mill in 1993,[20] but it was not actual commitment of Daishowa.

In exchange for the concessions, 630 permanent jobs were expected to result from the FDI. The Alberta government emphasized to the constituency the creation of jobs in Peace River and the other economic benefits which would accrue to the region as well as to the province.[21] The FDI appeared promising to interests of the two parties: providing economic benefit to Daishowa and political benefit to the Getty government during the severe recession after the price declines of oil.

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[18] The Edmonton Journal, 4 August 1989, B7.

[19] The Globe and Mail, 9 February 1988. B1, B4.

[20] Nikiforuk and Struzik, 60.

[21] The Edmonton Journal, 9 February 1988, F1.

## The Challenge from Environmentalists

### (1) Dioxins Issue

One Daishowa general manager emphasized how the emergence of the anti-Daishowa pulp mill environmental movement was "sudden",[22] but the basis of the movement already existed before the deal was finalized. In the 1980s, environmental movements gained a certain degree of political power in Europe and, to a lesser extent, in North America. In Canada, a series of domestic and international environmental disasters fueled the environmental protest.[23] Environmentalists argue that no toxic substance should be released into the environment, because the hazards to human health of the accumulation of toxic substances in the environment are not fully understood.[24]

Concern among Canadians over cancer-causing dioxins, which are contained in discharge from bleached pulp production, had been increasing since the early 1980s. After the discovery of high levels of dioxins in the discharge from pulp mills in the Great Lakes region, environmentalists criticized the government of Canada for its lenient regulation of the pulp and paper industry. Owing to its importance to Canada's economy,[25] the industry made use of an environmental policy-making system which was closed to the public; they gained tolerance from the governments in Canada.[26] However, the record of the industry as a "consistent violato(r)" of environmental regulations and as "one of Canada's largest polluters"[27] enhanced the public's concern. By 1988, "the issue of pulp mill dioxins was given a new urgency in Canada."[28]

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[22] Morrison, interview by author, Edmonton, Alberta, 30 April 1992.

[23] Doug Macdonald, The Politics of Pollution: Why Canadians Are Failing Their Environment, (Toronto: McClelland & Stewart Inc., 1991), 111-116.

[24] Ibid., 65.

It seems inevitable in hindsight that Daishowa's bleached kraft pulp mill would be targeted by environmental groups; nevertheless, the regulations applied at the mill were the strictest in Alberta at the time.

Opposition to the mill also came from other quarters. Under Canada's federal system, governments sometimes encounter interference from other governments in their jurisdictions, and must defend the legitimacy of their actions and decisions.[29] In this context, negative comments about a government's polices can have considerable influence. The government of the Northwest Territories, which has jurisdiction over a portion of the Peace River, expressed concerns about the contamination of the river by dioxins from the mill.

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[25] Globe and Mail, 16 March 1989, A1, quoted in Frank J.Tester, "Canada and the Global Crisis in Resource Development," 407 in Daniel Drache and Meric S. Gertler, The New Era of Global Competition : State Policy and Market Economy, (Montreal: McGill-Queeen's University Press, 1991), 407; the industry is the second largest exporter among Canadian manufacturer industries, Canadian Pulp and Paper Association, From Watershed to Watermark, (Montreal, 1987), quoted in Macdonald, The Politics of Pollution, 225.

[26] Ted Schrecker, "The Mobilization of Bias in Closed Systems: Environmental Regulation in Canada," Journal of Business Administration, Volume 15, 1984/85, 45-46.

[27] Ibid., 46.

[28] Macdonald, 233.

Within governments, departments have mandates and agendas of their own. The Alberta Department of the Environment, which has jurisdiction over environmental issues, was critical of the government's promotion of pulp mills.[30]

### (2) Forest Conservation

Environmentalism asserts that there is "a public interest in the fate of the forest"[31] and that management of forests should be carried out in such a way as to conserve the forest for the public interest. Environmentalists attacked Daishowa's logging method, clear-cutting, in spite of the fact that the company reforested in the manner specified by the Forest Management Agreement (FMA) between the company and the

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[29] Richard Simeon and Ian Robinson, State, Society, and the Development of Canadian Federalism, (Toronto: University of Toronto Press, 1990), 290-291.

[30] The Alberta Department of the Environment, Environmental Views, Volume 12, Number 2 (September 1989), 5-19.

[31] Wayne P. Grant, "Forestry and Forest Products," in W. D. Coleman and Grace Skogstad, eds., Policy Communities and Public Policy in Canada, (Ontario: Copp Clark Pitman Ltd., 1990), 132.

Alberta government.

### (3) Court Cases

Environmental groups often bring suit against governments over what they consider to be inadequate environmental regulations. In Alberta, the anti-Daishowa pulp mill groups brought three lawsuits against Alberta and/or the federal government from 1990 to 1992.[32] According to the company, the cases involved Daishowa, cost it money and time, and injured its reputation.[33] But since the governments did not lose any of the cases, no direct damage was done to the conditions of Daishowa's FDI as previously defined. One could argue that litigation was a poor strategy for the environmental groups, which could not afford to pay court costs if they lost.

### (4) The Influence of ALPAC

It could be said that an additional investment in pulp and paper in Alberta enhanced the environmental movement's attack against Daishowa. In spite of increasing opposition to

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[32] These lawsuits were as follows: an environmental group versus the federal and Alberta government agencies regarding the lack of "full environmental review" of the Daishowa's mill, The Edmonton Journal, 21 February 1990, A8; three environmental groups versus the Alberta Ministry of Forest Land and Wildlife regarding the inadequacy of the forest management agreement with Daishowa, Alberta Wilderness Association, "Daishowa Forest Management Lawsuit Information for Press Conference," 30 September 1991; Four environmental groups and one native group versus the Alberta Minister of the Environment regarding the provision of the business license to Daishowa, The Edmonton Journal, 14 January 1992, A5.

[33] Morrison, transcript of speech, "Daishowa's Alberta Operations," 15.

Daishowa's mill, the Alberta government announced another bleached kraft pulp mill; Alberta-Pacific Forest Industries Inc. (ALPAC), a joint venture of Japanese paper producers and the Sogoshosha, planned to construct the world's largest scale bleached kraft pulp mill[34] near Athabasca north of Edmonton. About 300,000 Albertans signed petitions against this project, asking the government to stop not only the project itself, but all promotion of the pulp manufacturing industry.[35]

Whenever a "rivalry" between an MNC and its host government has been made public in the developed states, "the MNC has received condemnation in the media and in other public discourse."[36] And when the public find that they are being deceived by the MNC, or that they are suffering from damages caused by the MNC, the MNC is also condemned publicly in the media. The federal government of Canada, which holds jurisdiction over rivers that flow through more than one province, involved itself in the review of the environmental impact assessment (EIA) report on ALPAC's proposed mill. It found deficiencies in the report and ordered a review of the company, although the Alberta government accepted the report.[37] It could be said that part of the public thought

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[34] Nihon Keizai Shinbun (Japan Economic Newspaper), 15 December 1988.

[35] Nikiforuk and Struzik, 64.

[36] Kudrle, 231-232.

[37] Macdonald, 237-238.

ALPAC attempted to cheat Albertans; as a result, the public also questioned the pollution control of Daishowa's mill. Their doubt was fueled by several facts: the review of Daishowa's assessment was made only by the Alberta government; there were no public EIA hearings on Daishowa, as there had been on ALPAC; the ministerial hearing about the project was waived by the cabinet.[38]

### (5) Daishowa's Response

Responding to intense pressure from the anti-mill movement, Daishowa took the following measures and attempted to influence opinion in Alberta. These measures targeted mainly urban citizens in the province who were either against the development or concerned about deterioration of the environment by the mill. On the contrary, the local constituencies in Northern Alberta are very supportive of not only Daishowa's mill but also the entire pulp mill development plan of the Alberta government in Northern Alberta because of increases of employment, population growth[39] and a better industrial tax base. Daishowa took advantage of this support to reinforce its bargaining power against the anti-mill movement.

In order to show its awareness of environmental issues, Daishowa established an advisory committee which consisted of local environmental groups and the company, and supported it financially.[40] The company participated in a program of the Albertan forest industry established to deal with the forest-conservation movements.[41] In order to win the public's trust, Daishowa emphasized its high-tech environmental protection system.[42] It urged the media not to provide misinformation.[43] Needless to say, Daishowa stressed its economic contribution to Alberta. It also acted on the Japanese government's general advice to Japanese investors in North America and Europe, engaging in philanthropy and active participation in its subsidiaries' local communities.[44]

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[38] Nikiforuk and Struzik, 60.

[39] John Sheene, spokesman of Friends of the Peace, environmental group, interview by Kathleen Stokes and author, Peace River, Alberta, 9 May 1992.

## The Daishowa-Lubicon Issue

### (1) History of the Lubicon Land Claims

The hardships of the Lubicon Indians began with their treatment by Canada's federal government. The federal government has jurisdiction over Indian reserves in Canada. In exchange for ownership of their land, Canada provides

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[40] Morrison, transcript of speech, "Daishowa's Alberta Operations", 9: Wayne Crouse, Communication Coordinator, Daishowa Canada, Co., Ltd., interview by Kathleen Stokes and author, Peace River, Alberta, 9 May 1992.

[41] Morrison, transcript of speech, 1.

[42] Crouse, interview by Stokes and author.

[43] Morrison, interview by author.

[44] The JETRO (Japan External Trade Organization), 1992 JETRO Hakusho Toshi Hen: Sekai to Nihon no Kaigai Chokusetsutoshi (1992 JETRO White Paper Volume Investment: World and Japanese Foreign Direct Investment, (Tokyo: The JETRO, 1992), 126.

Natives with reserve-land determined by the band's membership on the band list; the government also provides protection and social services to Native individuals.[45] Thus the band list is the centrally important document that assures Natives of their right to receive social services[46] and determines the areas of reserves. In the early 1940s, the Canadian government deleted almost half of the Lubicon Indians from the band list in order to cut its federal expenditure.[47] The government did not give the band its promised reserve.[48] When Alberta planned to develop the oil found in regions of the province including this land, the provincial government asked the federal government whether it had to leave the land untouched, since Canada had once promised the area to the Lubicon. The federal government did not answer Alberta's query. Since then, the land promised the Lubicon has been the property of the Alberta government.[49]

Alberta's relationship with Native people is described as

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[45] G. Brown and R. Maguire, Indian Treaties in Historical Perspectives, (Ottawa: Department of Indian Affairs and Northern Development, 1979), XVII-XXIV, quoted in Hiroaki Kato, Tagen Kokka Kanada no Jikken: Renpo Shugi, Senjumin, Kenpo Kaisei (Pluralistic State Canada's Experiment: Federalism, Aboriginal People, Constitutional Amendment, (Tokyo: Sanseido Shoten, 1990), 95.

[46] The Edmonton Journal, 17 November 1991, E3.

[47] John Goddard, Last Stand of the Lubicon Cree, (Toronto: Douglas & Mcintyre, 1991), 7-31.

[48] Globe and Mail, 27 December 1991, A4.

[49] The Edmonton Journal, 17 November 1991, E3.

"adversarial."[50] The Alberta government acted as if it believed the Lubicon "ha(d) no right whatsoever to impede development of the natural resources", even on their claimed land.[51] Rapid development of the oil industry, which proceeded with "no environmental or social-impact studies" in the promised reserve area from the late 1970s to the early 1980s, wreaked havoc in the lives of the Lubicon.[52]

The Lubicon already had a long history of political negotiation with the federal government and the government of Alberta. Federalism hindered progress of the Lubicons' negotiation. In these talks, the band asked for a restoration of erased band memberships, the provision of reserve land based on the number of the Lubicons, and compensation money for the hardships caused by the two governments. Unanimous agreement between the three governments was difficult to attain. Basically, the governments of Alberta and Canada each tried to avoid bearing any more blame than the other. The federal government feared making a precedent for other native land claims at a time when the Canadian native peoples were gaining political power as an interest group in the late 1980s.

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[50] James O'Reilly, "Indian Land Claims in Quebec and Alberta," in J. Anthony Long and Menno Boldt, eds., Governments inConflicts? : Provinces and Indian Nations in Canada, (Toronto: University of Toronto Press, 1988), 147.

[51] Ibid., 147.

[52] Goddard, 74-75.

### (2) Involvement of Daishowa

The traditional area of the band was overlapped and the prospective reserve area was encompassed by Daishowa's forest management area.[53] Why did Daishowa take the risk of becoming involved in the Lubicon dispute? It was said that the government of Alberta told Daishowa the issue would be solved before the firm actually made its FDI, and that the exclusion of the future reserve area would be enough to secure Daishowa's right to log.[54] The government did not feel any necessity to consult the band. Needless to say, the promised access to the aspen stands, as well as the other concessions, were attractive to Daishowa. For Daishowa, the desire to secure its supply of raw materials and maximize its profit through this FDI came before any consideration of the risk to the Lubicon, or of the band's human rights.

Daishowa faced antagonism from the band and a considerable amount of public criticism, and finally it had to cancel its plans for clear-cutting on the Lubicon's traditional land. The official announcement of the FDI outraged the band and raised public condemnation against Daishowa and the Alberta government. Timing also affected the reaction. The announcement came immediately after the Lubicon had achieved some success in their international campaign of publicity against the Alberta and federal governments. The

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[53] Nikiforuk and Struzik, 60.

[54] Morrison, interview by author.

Lubicon had been granted a United Nations Human Rights Committee hearing on the situation of the band, and had launched a boycott of the Calgary Olympics.

While the Lubicon's negotiations with the federal government stagnated, Daishowa made a plan for to begin logging in the traditional lands in the winter of 1990. The Lubicon claimed the logging would cause environmental damage, further degrading their lives, and that it would weaken their bargaining power with the Alberta and federal governments.[55] Their representatives asked the company to abandon the plan and warned that the band would stop the cutting by any means necessary. Facing strong opposition from the band, which had won public support, the firm had to agree to a moratorium on the plan. The following year, it had to accept another moratorium on a logging plan because the band began an international boycott of its products. The firm hoped to avoid worsening the Daishowa-Lubicon conflict.

In January 1992, Daishowa officially announced it had cancelled construction of the second mill because of its conflict with the Lubicon, but the real reason for the cancellation was financial difficulty caused by the huge debt[56] of the firm's parent company.

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[55] The cutting would imply: the band's *de facto* recognition of the action taken by Alberta and the federal government -- the invitation to Daishowa to engage in FDI-development of their claimed land without any consultation with the Lubicon; the band's retreat from its position in requesting compensation money for the oil "taken from" its land, because the trees were also a natural resource of the land.

### (3) The Influence of Canadian Federalism

The jurisdictional arrangements of Canadian federalism became troublesome to Daishowa. The federal government, which does not have jurisdiction over the economies of provinces, was much less concerned about Daishowa's awkward position. The government repeatedly stalled the progress of negotiations with the Lubicon. Furthermore, it made a "take-it-or-leave-it" offer to the band[57] after Daishowa invested in Alberta. It could be said that this offer resulted in strengthening the anti-Daishowa movements by the band, because the band had opportunities to take advantage of public notice to and sympathy for its anti-Daishowa actions in order to increase public support for its stance in the negotiation with the federal government.

### (4) Unreconciled Interests

It was difficult for Daishowa to meet Lubicon demands. They ran contrary to the most important purpose of Daishowa's FDI -- obtaining security of tenure over the raw materials needed for the pulp mill over a lengthy period. If Daishowa complied with the demand that it desist from cutting on the area of 10,000- square-km[58] which the band claimed as its traditional land, part of the capital invested in the mill would be at risk of being wasted. In addition, planned flow of raw materials in Daishowa's vertically-integrated global production system would require adjustment. If it complied, the company's hope of significantly reducing production costs to the Daishowa group by operating the Peace River mill[59] would not be realized. Daishowa was more dependent than other major Japanese paper producers on pulp sold on the world market, where prices fluctuate greatly; the so-called pulp cycle meant that the Peace River mill was important for the Daishowa group to stabilize its cost of pulp at lower prices. In addition, Daishowa was deeply committed to the operation of the mill because it represented the company's first 100 percent owned, non-acquired FDI. 100 percent ownership of FDI means full control of management, and more profit from the FDI to the MNC(and, of course, all of the risk). Besides these business considerations, uncertainty about the outcome of Lubicon's negotiations with the federal and provincial governments made it difficult for Daishowa to take definite measures to deal with the demands. It was not clear when the negotiations would end or how large the Lubicon reserve would ultimately be.

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[56] Nihon Keizai Shinbun(Japan Economic Newspaper), 6 April 1991.

[57] Goddard, 198.

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[58] The Edmonton Journal, 7 October 1990, A5.

[59] Nihon Keizai Shinbun(Japan Economic Newspaper), 25 July 1989.

### (5) Daishowa's Response

Daishowa was defensive in its dealings with the band and the public, and passive toward the provincial and federal governments regarding the Daishowa-Lubicon issue. Daishowa called itself "a third party in good faith"; it emphasized that it was not able to solve the dispute between the band and the two governments, but that it had the right to log in those areas defined by the FMA with Alberta which excluded the prospective reserve area. Daishowa was not competent to deal with the "politicized" conflicts between the Lubicons and the governments. But, in addition to negotiating with the company about the disputes that arose between the company and them, the Lubicons also made use of Daishowa to promote their interests in the negotiations with the provincial and federal governments. Daishowa expressed its position through the media, but compared with the Lubicon's intensive anti-cutting campaign, including the Daishowa boycott, Daishowa had difficulty reaching the public. The company lobbied the governments to hasten negotiations with the band, but to little effect. The deadlocks continued.

## Responses of the Alberta Government to Daishowa's Trouble

The bargaining power of an MNC is at its greatest before actual FDI is made, owing to the technology, expertise and marketing ability which it offers. Host states are anxious to develop the industry represented by the MNC as well as the whole national economy. The MNCs have to accept certain risks of FDI. Consequently, host states grant concessions to the MNCs.[60] In the case of Daishowa's FDI, the Alberta government's strong desire to promote the forest industry in a severe recession was an additional factor leading the Alberta government to make concessions.

In addition, since the nature of the relationship between MNCs and host governments is that of "joint-maximization" -- a non zero-sum game -- the two agents adopt "collaborative strategies" to "increase the size of the pie to be divided and increase the absolute returns" to them both.[61] The Alberta government took a cooperative stance in the early stages of the Daishowa-Lubicon dispute.

The bargaining power of a host state often increases after FDI is actually made, because the foreign investor has committed its investment. Consequently, the host state can avoid making further concessions to the MNC.[62] Domestic groups whose interests conflict with those of the MNC put pressure on the firm. As a result, they lessen the MNC's bargaining power with the host state. Because of changes in the power-balance, the host states can easily apply policies to the MNCs which are the "outcome" of contestation with domestic groups.[63] In Daishowa's case, the alterations of the power-balance before and after the actual investment as well as the pressure from environmental groups, the Lubicon and the public, preceded the shift of power.

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[60] Moran, 159.

[61] Ibid., 158.

[62] Ibid., 160-161.

[63] Ibid., 169.

### (1) Responses to the Environmental Issues

The increased bargaining power of the Alberta government was reflected in changes to the government's environmental policy in 1990 and 1992. In spite of the fact that the agreement between Daishowa and the government stated the prospective construction of another pulp mill, the company was not consulted about the changes.[64] The government changed the structure of decision-making on environmental regulations from a "closed system"[65] to one which would encourage more public participation.[66] New projects relating to natural resources, including those in the forest industry, became subject to formal public hearings. This new situation was radically different from what Daishowa had dealt with in the construction of its first mill, when there had been no public hearing on the EIA and the cabinet had waived the ministerial hearing.

The Daishowa's existing mill was not subject to the new regulations, and there was no change in the regulatory standards applied to the mill. But "modest successes" of host states in changing" the behavior of multinationals" "are useful"[67] to the interests of the host states, because "they provide a base upon which future changes can be built incrementaly."[68] Daishowa alleged that the changes would negatively affect its plan for the second pulp mill, since public participation in the Environmental Impact Assessment of ALPAC had made the standards applied there more strict. The company also claimed that the potential cost in time and money it would incur as a result of public intervention would be an obstacle to Daishowa's business plan for the second mill.[69] More importantly, it was impossible to predict the consequences of public pressure. For Daishowa, there was new uncertainty in the environmental politics of Alberta. The firm also counted this among the reasons for cancelling its plans for a second mill,[70] although the main reason, as stated above, was the financial difficulty of the parent company.

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[64] Morrison, interview by author.

[65] Macdonald, 174.

[66] The oil and gas industries were excluded from the hearing since they were subject to a different board, the Alberta Department of the Environment, Environment Views, Vol. 13, No. 4 (Spring 1991), 5.

### (2) Response to the Daishowa-Lubicon Conflict

Soon after the announcement of Daishowa's project, Alberta premier Don Getty entered into the negotiations between the Lubicon and the federal government. It was speculated that Daishowa threatened the Alberta government, saying the company would cancel the FDI unless the Lubicon disputes were settled. Since the firm's FDI was very important to the economy of the province, premier Getty himself participated directly in the negotiations, in the hope of finding solutions.[71]

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[67] Peter Evans, "Multinational Strategies and Dependent Development," in Kendall W. Stiles and Tsuneo Akaha, 223.

[68] Evans, 223.

[69] Morrison, interview by author.

[70] Morrison, interview by author.

When FDI is made in capital-intensive industries, the bargaining power[72] of the host state increases after facilities are actually constructed. The Alberta government continued to say, "Daishowa is legally assured to cut the trees in its FMA area," though the Lubicon requested the cancellation of the cutting plan, after the construction of the mill. It did so in spite of the fact that relations between Daishowa and the Lubicon were getting worse. Prior to the moratoria, Daishowa received no consultation or advice concerning them.[73] When the official announcement of the cancellation was made, Alberta's deputy minister of Forest Services announced that the government was considering providing Daishowa with other areas for logging.[74] Ultimately, the MNC was not given any other land.

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[71] Nikiforuk and Struzik, 63.

[72] Moran, 160.

[73] Morrison, interview by author.

[74] The Edmonton Journal, 7 October 1990, A5.

## Responses of Japanese Government

"Although the promotion of new raw materials investments has not usually involved much disagreement between private actors and the state -- indeed, specific ventures rarely came to the attention of central decision-makers -- the protection of projects once they have actually been established has been a much more vexing problem." Host states, at one extreme, sometimes nationalize MNCs. MNCs' calls for protection by their home states are often rejected because the cost of the protection in economic, diplomatic and military terms is excessive compared with the economic benefit of, say, securing raw materials.[75]

In the case of Daishowa's FDI, protective action on the part of the Japanese government was not forthcoming. This was in spite of the fact that the government has promoted the FDI of the Japanese pulp and paper industry, one of the resource-consuming and polluting industries which were thought no longer appropriate to the industrial structure of Japan. A manager of Daishowa even confirmed that no consultations had taken place between Daishowa and the Japanese government, and that the government had given the firm no advice on how to deal with the environmental and Lubicon issues.[76] Japan's consul in Edmonton reported that the consulate discussed several matters with the company in the same way that it deals with other Japanese multinationals in its jurisdictional area.[77]

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[75] Stephen D. Krasner, Defending The National Interest: Raw Material Investments and U. S. Foreign Policy, (Princeton: Princeton University Press, 1978), 137.

[76] Morrison, interview by author.

"Most states at most time pay some respect to the basic rules of coexistence in international society," which include "mutual respect for sovereignty."[78] States respect their mutual sovereignty in their relations and do "not intervene forcibly and dictatorially in one another's internal affairs."[79] The Lubicon's disputes with Alberta and the federal government were Canada's internal affairs; the Japanese government did not intervene in the conflict, regardless of the trouble of Daishowa. The consulate attributed its avoidance of this issue to the principle of non-intervention.[80]

## Conclusion

Daishowa wanted to secure raw materials and maximize profit in Alberta. The first interest was typical of Japanese pulp and paper manufacturers, and the second was a common feature of all MNCs. The interests contested the interests of environmentalists, the Lubicons and the public, who became concerned about the environment and the situation of the Lubicon. The company's environmental philosophy was challenged by the anti-Daishowa environmental movement. Observation of the environmental regulations and the provincial logging regulations was not enough to convince the environmentalists. The company took measures to deal with the movement. It miscalculated the risk of its involvement in the Lubicon's land claim and ignored the Lubicon's human rights, in its pursuit of profit from FDI in Alberta as a part of its vertically-integrated global production system. As a result, it came to contend with the Lubicon for its right to cut in the band's claimed territory. The dispute with the band finally forced the company to compromise with the band.

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[77] Jun-ichi Kawamoto, Consul, Consulate-General of Japan, Edmonton, Alberta, interview by author, 29 April, 1992

[78] Hedley Bull, The Anarchical Society: A Study of Order in World Politics, (New York: Columbia University Press, 1977), 42.

[79] Ibid., 70.

[80] Kawamoto, interview by author.

Daishowa's bargaining power with the Alberta government was weakened in two ways. Pressure from the environmentalists, the Lubicon, and the public, who actively supported the latter two groups, weakened the company's bargaining power. The Alberta government was now facing competing pressure over its forestry policy. Second, the bargaining power of most companies that make FDI becomes weaker after their actual investment. In Daishowa's case, this was demonstrated by a series of incidents. After the company's actual investment, the Alberta government adopted new environmental policies which could adversely affect the environmental-impact assessments of Daishowa's prospective FDI. The government did not help Daishowa out of its scrape with the Lubicon, regardless of the FDI. In spite of Daishowa's compromise with the Lubicon, the government did not adopt any policy of compensation for the company. This disregard for Daishowa's difficulties was significantly different from the one the government had taken when it was making concessions before the FDI.

The Japanese government, which promoted the FDI of the pulp and paper industry, did not support Daishowa in its time of difficulties. The cost to the government of any protective action was too high in relation to any possible gain. Particularly in the case of the Daishowa-Lubicon dispute, the principle of non-intervention in the international society, as well as the Japanese government's aversion to influencing the domestic politics of Canada, made the government refrain from taking action.

Daishowa's case demonstrated that coping with environmental movements while securing raw materials overseas would become increasingly demanding to the Japanese pulp and paper industry, and that the FDI of other Japanese resource-consuming and pollution-causing industries would face the same problem. Those industries have made FDI in order to escape strict Japanese environmental standards and take advantage of the more lenient regulations of host states. Another purpose of the FDI made by those industries is securing raw materials for consumption. Therefore, it is logical and probably inevitable that they would face opposition from local environmental movements.

Technological developments might reduce the levels of pollutants effused by industries and might slow the overwhelming consumption of natural resources; however, the cost of adopting the technology could also discourage MNCs' voluntarily introducing it in their FDI. Strong pressure from the host governments might force the MNCs to adopt the technologies. But if the FDI of the MNCs is very important to the economy, the host government will refrain from demanding too much, because at one extreme, a MNC may withdraw its investment in order to avoid paying the high cost of introducing new technology.

What may break this deadlock in the developed states is pressure on MNCs and governments from the environmentally-aware public, as seen in Daishowa's case. The pressure would decrease the bargaining power of the MNC. Furthermore, the public might take advantage of the normal changes in the power balance between the MNC and the host government, which tend to favour the host government after the MNC's actual FDI.

Daishowa's case also demonstrates that one of the purposes of Japan's FDI policy, to transfer pollution-causing and resource-consuming industries abroad, would be increasingly criticized. The Japanese government hoped to strengthen the national economy by revising its comparative advantage, and thus to stop further destruction of the domestic environment. In the competitive international economy, states adopt FDI policies in order to promote their national economies. But policies that lead to environmental damage in host states and promote the consumption of natural resources beyond the limit of sustainable development are becoming unacceptable not only in the host states, but also in the international community. The Japanese government encourages the Development and Import (D & I) strategy to cope with resource scarcity. But the operation of D & I would also face difficulties since it would be expected to accord with the idea of sustainable development in the host state.

## CHAPTER SIX - Conclusion

This thesis has discussed important features of the development of Japanese foreign direct investment(FDI), and studied important issues pertaining to Japanese FDI through a case study of a Japanese pulp and paper manufacturer in Alberta, Canada. This thesis concluded that the development of Japanese FDI since the end of the Second World War had been promoted by domestic factors which emerged from structural changes of the Japanese economy, which were largely the result of the industrial policies of a strong economic-nationalist Japanese government. These structural changes drove the historic high-speed economic growth.

However, changes in the international sphere have gained increasing influence on the development of Japanese FDI since the 1970s. The reason for this is that the Japanese economy has been integrated into the international economy, with step-by-step deregulations of Japan's economic policies; and national economies have become more interdependent.

It was also concluded from the case study that the Japanese FDI to compensate for resource-scarcity in Japan, i.e., to secure natural resources for industries of Japan, and to transfer pollution-causing industries, has faced and will face opposition from the people of host developed/developing states and criticism from the international society. This conclusion was reached because public awareness of environmental issues has been rising and environmental issues are important in national and international political economy.

The second chapter examined the applicability of theories of FDI to Japanese FDI. The examination showed that some features of Japanese FDI can be basically explained by the theories based on studies of business activities of Western multinationals (MNCs), but supplemental theories are necessary to explain important features of Japanese FDI which differ from those of Western FDI. The important features are: (1) much Japanese FDI has been made in developing states to employ cheaper labor; (2) many small- and medium-sized Japanese firms have made FDI.

Product cycle theory and industrial organization theory were examined with regard to their applicability to Japanese FDI. The supplements to the product cycle theory emphasized the fact that Japanese industrial manufacturers entered in the later phase of the production cycle. In the later phase, technologies for production are already standardized and can be handled by unskilled labor. Therefore, reducing the labor cost is important to the manufacturers in the later phase. In contrast in the earlier phase, newly developed technologies are difficult for unskilled labor to deal with; therefore, unskilled labor cannot be employed, and the cost for research and development is important. Reducing labor costs by making FDI in developing states was critical for the Japanese manufacturers.[1]

The industrial organization theory is applicable to the FDI made by Japanese industrial manufacturers in developed states because the manufacturers were oligopolistic firms and possessed the firm-specific advantages which were attributed to the MNCs by the theory. However, the theory has a difficulty in explaining the FDI made by Japanese firms lacking the firm-specific advantages.

The chapter also examined the theory of Japanese FDI developed by Kiyoshi Kojima that Japanese FDI serves as a "tutor" to foster industries in the developing host state.[2] It was concluded that this theory is not proven.

Another important argument made in this second chapter is that Japanese FDI was a way of compensating for scarcities of production factors, which were defined by some economists as inevitable scarcities from rampant industrialization in the long run.[3] This argument was based on the facts that high economic growth resulted in: 1) rapid wage increases for Japanese workers, 2) labor shortage, 3) and an exacerbation of resource scarcity. These three conditions promoted increases in Japanese FDI in the form of 1) Japanese labor-intensive industries' FDI in the developing states employing cheap and abundant labor, 2) the resource-consuming industries' FDI in resource-producing states.

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[1] Terutomo Ozawa, Multinationalism, Japanese Style, (Princeton: Princeton University Press, 1979), 50.

[2] Kiyoshi Kojima, Nihon no Kaigai Chokusetsutoshi(Japanese Foreign Direct Investment), (Tokyo: Bunshodo, 1987), I.

[3] Ozawa, 66.

Serious pollution was brought about by rapid growth of heavy and chemical industries, which were encouraged by the government as leaders of economic growth. Pollution at home eventually forced polluting industries to move their operations abroad.

The third chapter argued that while domestic factors exerted much influence on the development of Japanese FDI to the 1970s, international factors have exerted influence increasingly since the 1970s. In addition to the government's regulatory control over the in- and out-flows of capital, the industrial policies of the Japanese government were closely related to the growth of Japanese FDI. Rising wages for Japanese workers, made possible by economic growth, induced Japanese companies to make FDI in developing states in order to take advantage of cheap and abundant labor. Small- and medium-sized Japanese firms in labor-intensive industries made FDI there in large numbers. Government support of heavy and chemical industries resulted in greater resource-scarcity and compelled industries to make FDI in resource-producing states. The Japanese government have encouraged this type of FDI. It so did especially after the first oil crisis. Within this FDI, the Development and Import(D & I) strategy in which Japanese MNCs develop natural resources in resource-producing states and then import the resources was a better way for

Japanese resource-consuming industries to secure natural resources.

But the government-supported growth of heavy and chemical industries resulted in serious pollution. It raised strong opposition from residents around industrial sites against further expansion of the industries. As a result, the government enacted a stricter environmental policy. Opposition from the residents as well as tightened environmental regulations were the promotive factors of the growth of FDI in states with relatively lax environmental standards.

Since the 1970s, international factors have exerted more influence on the development of Japanese FDI. The main international factors were, 1) a dramatic rise in the value of the yen against the U.S. dollar in a short period: a result of the introduction of floating foreign exchange rates because of the relative decline of the status of the U.S. economy and by policy coordination among major national economies, i.e., the Plaza Agreement in 1985, 2) acknowledged vulnerability and resource scarcity by the Japanese industries and the Japanese government in the oil crisis in 1973 and 1979, and 3) the new protectionism from the United States and Western Europe against the large amount of the Japanese exports of manufactured goods. The new protectionism was expressed in the adversarial trade policies of governments and taken in reaction to pressure by those industries weakened by Japanese exports. These factors promoted increases in Japanese FDI in the following ways: 1) a strong yen made foreign assets cheaper, e.g., a pulp mill could be build by Japanese investors for 50 percent of its previous construction cost in the same host states; 2) the acknowledged seriousness of resource-scarcity factor promoted the FDI of resource-consuming industries, the Japanese government encouraging FDI of such industries, 3) industrial manufacturers facing the new protectionism made FDI in large scale in the United States and Western Europe to maintain the level of their sales to the customers there.

This chapter also argues that large Japanese trading companies, the sogoshosha, played promotive roles for the growth of Japanese FDI. The sogoshosha enabled smaller Japanese MNCs to make FDI.

The fourth chapter studied the development of the FDI of the Japanese pulp and paper industry as an example of the FDI of the Japanese resource-consuming and pollution-causing industries. In this chapter, it was argued that while domestic factors have influenced the FDI of such industries in the past, international factors are becoming increasingly important. It was also maintained that in the late 1980s the FDI of the industry started to take measures to cope with the rising pubic lobbying for conservation of forests by starting afforestation in FDI.

The industry grew steadily and faced a shortage of lumber, which was made worse by the state-led economic growth. However, the industry solved the problem by increasing the import of wood chips. This continued to enhance the dependency of the industry on overseas suppliers. In the meantime, the pollution issues caused by the industry in Japan became a potential promotive factor for the industry's FDI, but weakened position of the industry which was brought about by the 1973 oil crisis limited FDI. In 1980, the dependency of the industry proved seriously detrimental to its relations with the overseas suppliers, forcing it to accept huge, unilateral price hikes. FDI came to be seen by Japanese industry and government as a better way to secure raw materials. However, stagnant business conditions in the early 1980s, made worse by another oil crisis and by the Iranian Revolution, made full scale FDI of the industry prohibitive. However, finally, international events as well as domestic factors resulted in the industry's full-scale FDI by the mid-1980s. But shortly thereafter, public awareness of environmental issues in international forestry posed obstacles to the expansion of FDI of the industry. The rising awareness led the whole industry to start afforestation in their FDI in the 1980s.

The Daishowa case study in chapter five showed the determinants of this particular FDI and the issues which took place in relation to this FDI in Alberta. International factors influenced the decision to make the FDI a great deal.

The features of the pulp and paper industry which are resource-consuming and pollution-causing posed difficulties for Daishowa's FDI. The public concerns about environmental issues raised opposition against the business operation of the FDI, pulp-making. In addition, a peculiar Canadian issue, a native land claim, became a controversial issue in the FDI. This issue also bore the imprint of environmental issues. The attitude of the host government, the Alberta government, changed radically before and after Daishowa's making its actual FDI because the balance of bargaining power between Daishowa and the Alberta government shifted over time.

This chapter also argued that coping with environmental movements abroad would increasingly raise demanding issues in their FDI for the Japanese pulp and paper industry as well as the other resource-consuming and polluting industries. This was because despite the fact that public opposition to exploitation of natural resources and pollution grew too great to ignore, the main objectives of these industries' FDI include securing raw materials and moving abroad in order to avoid strict Japanese governmental environmental standards .

It was also concluded from the case study that the purpose of Japanese FDI policy to secure raw materials and export pollution would face the same opprobrium abroad as Japan's industries faced at home. International censure would be an additional burden. Even Development & Import(D & I), which is an effective way to secure natural resource for

Japanese industries, would be hard to implement because any development would be required to accord with the concept of sustainable development in the states.

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APPENDIX 1: (TABLE 1)

Japanese Foreign Direct Investment by Region: 1951-1988
(Percentage)

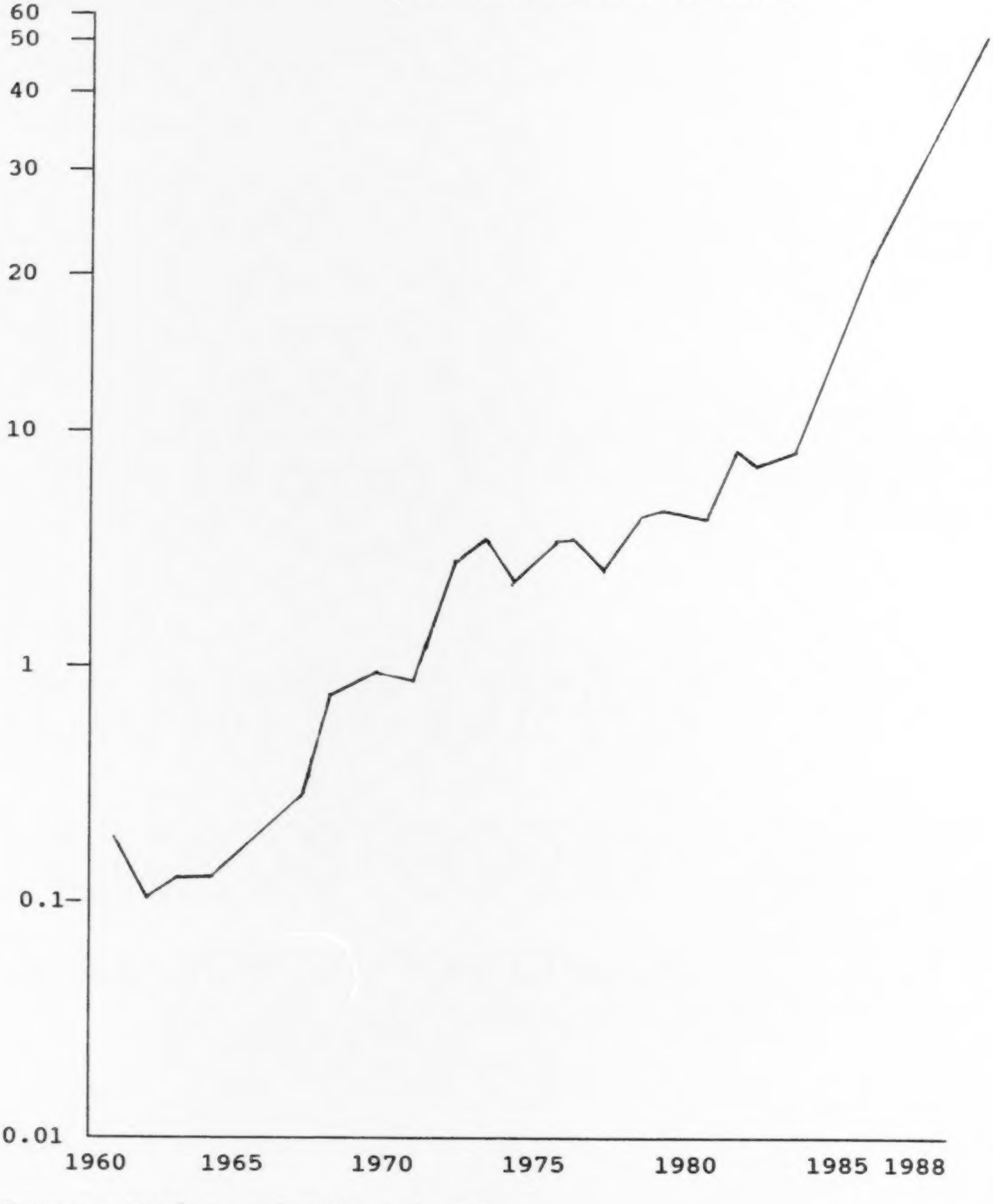
| | 1951-1960 | 1961-1970 | 1971-1975 | 1976-1980 | 1981-1985 | average 951-1985 | 1986-1988 |
|---|---|---|---|---|---|---|---|
| North America | 31.1 | 25.0 | 24.3 | 28.6 | 36.4 | 32.2 | 46.9 |
| United States | 30.7 | 18.6 | 22.0 | 26.6 | 34.8 | 30.2 | 45.3 |
| Asia | 17.3 | 21.3 | 28.1 | 27.3 | 20.4 | 23.3 | 12.4 |
| Asian *NIES | 4.6 | 5.0 | 10.2 | 10.2 | 8.7 | 9.1 | 7.2 |
| *ASEAN | 9.2 | 13.1 | 17.6 | 16.8 | 10.8 | 13.4 | 3.5 |
| Europe | 1.1 | 19.3 | 15.2 | 9.5 | 13.9 | 13.2 | 18.7 |
| Middle East | 19.9 | 8.4 | 5.2 | 6.2 | 1.5 | 3.6 | 0.4 |
| Oceania | 0.7 | 7.6 | 5.3 | 7.8 | 3.6 | 5.1 | 4.9 |
| Other Areas | 30.0 | 17.4 | 21.9 | 20.6 | 24.2 | 22.7 | 16.7 |

Source: Komiya and Wakasugi, 52.

*NIES = Newly Industrializing Economies
*ASEAN = the Association of South East Asian Nations

APPENDIX 2: (FIGURE 1)

Japanese Foreign Direct Investment, 1960-1988
( in U.S. billion dollars)



Source: Komiya and Wakasugi, 50.

APPENDIX 3: (TABLE 2)

Japanese Foreign Direct Investment by Region (in U.S. million dollars)

| | North America | Western Europe | Asia | Latin America | Oceania | Africa | Middle East |
|---|---|---|---|---|---|---|---|
| 1975 | 905 | 333 | 1,110 | 327 | 182 | 338 | |
| 1976 | 749 | 337 | 1,245 | 420 | 162 | 550 | |
| 1977 | 735 | 220 | 865 | 456 | 165 | 365 | |
| 1978 | 1,364 | 323 | 1,340 | 616 | 239 | 717 | |
| 1979 | 1,438 | 495 | 976 | 1,207 | 582 | 168 | 130 |
| 1980 | 1,596 | 578 | 1,186 | 588 | 448 | 139 | 158 |
| 1981 | 2,522 | 798 | 3,338 | 1,181 | 424 | 573 | 96 |
| 1982 | 2,905 | 876 | 1,384 | 1,503 | 421 | 489 | 124 |
| 1983 | 2,701 | 990 | 1,847 | 1,878 | 191 | 364 | 175 |
| 1984 | 3,544 | 1,937 | 1,628 | 2,290 | 157 | 326 | 273 |
| 1985 | 5,495 | 1,930 | 1,435 | 2,616 | 525 | 172 | 45 |
| 1986 | 10,441 | 3,469 | 2,327 | 4,737 | 992 | 309 | 44 |
| 1987 | 15,357 | 6,576 | 4,868 | 4,816 | 1,413 | 272 | 62 |
| 1988 | 22,328 | 9,116 | 5,569 | 6,428 | 2,669 | 653 | 259 |
| 1989 | 33,902 | 14,808 | 8,238 | 5,238 | 4,618 | 671 | 66 |

Source: Keizai Hakusho Showa 63 (Economy White Paper 1989), "Taigain Chokusetsutoshi Todokede Zandaka (Foreign Direct Investment Notified Amount)", (Tokyo, the Ministry of Finance, 1989), 471; Keizai Hakusho Heisei 2 (Economy White Paper 1990), "Taigai Chokusetsutoshi Todokede Zandaka (Foreign Direct Investment Notified Amount)," (Tokyo, the Ministry of Finance, 1990), 488.

APPENDIX 4: (TABLE 3)

## Production and Consumption of Paper and Paperboad by States in 1987

(in thousand tons)

| Production Total Rank | Name | Amt | Consumption per Capita Rank | Consumption per Capita Amt(Kg) | Consumption Total Amt | Consumption Total Rank |
|---|---|---|---|---|---|---|
| 1 | The United States | 67,544 | 1 | 305.6 | 74,488 | 1 |
| 2 | Japan | 22,537 | 9 | 184.8 | 22,589 | 2 |
| 3 | Canada | 16,046 | 4 | 218.5 | 5,594 | 9 |
| 4 | People's Republic of China | 11,411 | N/A | 11.5 | 12,427 | 3 |
| 5 | The Soviet Union | 11,036 | N/A | 38.0 | 10,486 | 5 |
| 6 | West Germany | 9,924 | 7 | 190.9 | 11,674 | 4 |
| 7 | Finland | 8,003 | 2 | 273.9 | 1,351 | 22 |
| 8 | Sweden | 7,881 | 3 | 238.9 | 2,005 | 18 |
| 9 | France | 5,832 | 18 | 130.1 | 7,262 | 7 |
| 10 | Italy | 4,987 | 21 | 103.8 | 5,948 | 8 |

Source: Asaoka, 10, Table 1-1, 11, Table 1-2, 12.

APPENDIX 5: (TABLE 4)

Growth of Production of Paper and Paperboard
(in thousand tons)

| Year | Paper | Paperboad |
|---|---:|---:|
| 1946 | 198 | 28 |
| 1955 | 1,834 | 590 |
| 1965 | 4,726 | 3,079 |
| 1975 | 7,711 | 5,890 |
| 1976 | 8,631 | 6,763 |
| 1977 | 8,759 | 6,943 |
| 1978 | 9,364 | 7,136 |
| 1979 | 9,981 | 7,880 |
| 1980 | 10,536 | 7,552 |
| 1981 | 10,943 | 7,037 |
| 1982 | 10,353 | 7,099 |
| 1983 | 10,932 | 7,510 |
| 1984 | 11,429 | 7,915 |
| 1985 | 11,790 | 8,679 |
| 1986 | 12,272 | 8,790 |
| 1987 | 12,807 | 9,730 |

Source: Yano Keizai Kenkyujo (Yano Economic Resreach Institutie Ltd.), Kami Palupu Sangyo (Pulp and Paper Industry), 156; the Ministry of International Trade and Industry, Tsusan Daijin Kanbo Chousa Tokei Bu (Reseach and Statistics Department of Secretariates to the Minster), Kami Palupu Tokei Nenpou (Pulp and Paper Statistics Report: 1985-1987), (Tokyo: the Ministry of International Trade and Industry, 1988), 24.

## APPENDIX 6: (TABLE 5)

Foreign Direct Investment
of the Japanese Pulp and Paper Industry in the 1980s

| Year | Japanese Company<br>Place | Company Name<br>Main Products<br>Production Capacity/Day<br>(in thousand tons) |
|---|---|---|
| 1986 | Kanzaki Paper<br>The United States Mass. | Kanzaki Specialty Papers Inc.<br>Thermo-printing Paper<br>Unknown |
| 1986 | Settsu<br>The Untied States Ga. | Carauster Industries Inc.<br>Paperboard from Waste Paper<br>450 |
| 1988 | Daishowa Paper<br>The United States Wash. | Daishowa America Co., Ltd.<br>Paper for Telephone Directory<br>100 |
| 1988 | Oji Paper<br>Canada B. C. | Howe Sound Pulp and Paper Co., Ltd.<br>*BKP<br>350 |
| 1988 | Daishowa Paper<br>Canada Alta. | Daishowa Canada Co., Ltd.<br>BKP<br>340 |
| 1988 | Daishowa Paper<br>Canada Que. | Daishowa Forest Products Ltd.<br>Newsprint<br>430 |
| 1988 | Settsu<br>Portugal, Lisbon | Matrena-Sociedade Industrial de Papeis<br>Printing Paper<br>10 |
| 1990 | Kanzaki Paper<br>Germany, Neümuhl | Kanzaki Spezial Papiera Gmb H<br>Thermo-printing Paper<br>25 |

| | | |
|---|---|---|
| 1990 | Daishowa Paper<br>Australia, Tasmania | *N/A<br>Non-bleached *L. KP<br>500 |
| 1990 | Daishowa Paper<br>The United States Cal. | N/A<br>Paperboard<br>N/A |

*BKP = bleached kraft pulp
*N/A = not applicable
*L. KP = hardwood kraft pulp

Source: Japan Paper Association, Kami Palupu: Kami Palupu Sangyo no Genjo (Pulp Paper: Present Conditions of the Pulp and Paper Industry, No. 512 (Special Issue 1992), 23; Asaoka, 134, Table 3-1, II; Nihon Keizai Shinbun (Japan Economic Newspaper), 12 April 1989, 14 July, 1989.